

VAVRINEK, TRINE, DAY & CO., LLP
(PLEASANTON OFFICE)

Review Report

For the Firm's Audits of
Emery Unified School District
for the Fiscal Years Ended June 30, 1998, 1999, and 2000;
Fremont Unified School District
for the Fiscal Year Ended June 30, 2000;
Newark Unified School District
for the Fiscal Year Ended June 30, 2000; and
Mission Valley Regional Occupational Program
for the Fiscal Year Ended June 30, 2000



STEVE WESTLY
California State Controller

August 2004



STEVE WESTLY
California State Controller

August 4, 2004

Linda S. Todd, CPA
Vavrinek, Trine, Day & Co., LLP
5000 Hopyard Road, Suite 335
Pleasanton, CA 94588-3351

Dear Ms. Todd:

The State Controller's Office (SCO) has completed a quality control review of Vavrinek, Trine, Day & Co., LLP (Pleasanton Office). We reviewed the audit working papers for the firm's audits of the Emery Unified School District for the fiscal years ended June 30, 1998, 1999, and 2000; the Fremont Unified School District for the fiscal year ended June 30, 2000; the Newark Unified School District for the fiscal year ended June 30, 2000; and the Mission Valley Regional Occupational Program for the fiscal year ended June 30, 2000.

A draft report was issued on June 8, 2003. After receiving the draft report, the firm's representatives requested that the SCO review additional documentation and information related to the findings. Additional information and documentation were provided at a meeting on August 4, 2003, and over the next three months. The findings were modified to reflect the results of the SCO's review and consideration of the additional information and documentation, and a revised draft report was issued to the firm's representatives on April 14, 2004, for their response. The firm's response to the revised draft report is included in this final report as Attachment 1. No changes were made to the findings as a result of the firm's comments. The SCO's comments regarding the firm's response are included as Attachment 2.

If you have any questions, please contact Casandra Moore-Hudnall, Chief, Financial Audits Bureau, at (916) 322-4846.

Sincerely,

A handwritten signature in dark ink that reads "Vincent P. Brown". The signature is fluid and cursive.

VINCENT P. BROWN
Chief Operating Officer

VPB:JVB/ams

cc: (See page 2)

cc: Sheila Jordan, Superintendent
Alameda County Office of Education
John Quinn, State Administrator
Emery Unified School District
John Rieckwald, Superintendent
Fremont Unified School District
John C. Bernard, Superintendent
Newark Unified School District
Charles Brown, Superintendent
Mission Valley Regional Occupational Program
Arlene Matsuura, Educational Consultant
School Fiscal Services Division
California Department of Education
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School Apportionment Specialist
Department of Finance

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Review Report

Summary

The State Controller's Office (SCO) has completed a quality control review of the audit working papers for the audits performed by Vavrinek, Trine, Day & Co., LLP, (Pleasanton office) of the Emery Unified School District (EUSD) for the fiscal years ended June 30, 1998, 1999, and 2000; the Fremont Unified School District (FUSD) for the fiscal year ended June 30, 2000; the Newark Unified School District (NUSD) for the fiscal year ended June 30, 2000; and the Mission Valley Regional Occupational Program (MVROP) for the fiscal year ended June 30, 2000. The last day of fieldwork was October 14, 2003.

Audits of local educational agencies are an essential element of public control and accountability. Auditing standards help to provide accountability and there is an expectation that, if the audit was performed in accordance with auditing standards, the audit will assist the user in making informed decisions.

The audits referred to above were performed in accordance with some elements of the standards and requirements set forth in *Government Auditing Standards*, issued by the Comptroller General of the United States, often referred to as generally accepted government auditing standards (GAGAS); generally accepted auditing standards (GAAS); Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*; and the *Standards and Procedures for Audits of California K-12 Local Educational Agencies* (K-12 Audit Guide), published by the SCO; however, many of the auditing standards and requirements were not met. The basis for the SCO's opinion is that the firm did not comply with many aspects of the general, fieldwork, and reporting standards. The testing of state compliance requirements of the K-12 Audit Guide and the single audit requirements of testing federal programs were not followed and/or adequately documented by the firm.

Background

Any governmental unit subject to a single audit must have the audit performed in accordance with the standards referred to in this report. According to OMB Circular A-133, the auditor's work is subject to a quality control review at the discretion of an agency granted cognizant or oversight status by the federal funding agency. In addition, *Education Code* Section 14504.2 authorizes the SCO to perform quality control reviews of working papers for audits of K-12 local educational agencies (LEAs) to determine whether audits are performed in accordance with U.S. General Accounting Office standards for financial and compliance audits.

Vavrinek, Trine, Day & Co., LLP, is an independent certified public accounting firm with an office located in Pleasanton, California. The Pleasanton Office performed 30 annual financial audits of LEAs for FY 1999-2000.

The firm was the independent auditor for EUSD for the fiscal years reviewed. Prior to July 2001, EUSD prevailed upon the State of California to provide an emergency apportionment loan as EUSD's financial standing was in severe jeopardy. In July 2001, AB 96, Chapter 135, Statutes of 2001, was signed by the Governor, and EUSD received a loan from the State. *Education Code* Section 14504.2(c) states:

If a school district has received an emergency apportionment pursuant to Article 2 (commencing with Section 41320) or Article 2.5 (commencing with Section 41325) of Chapter 3 of Part 24, the Controller shall conduct a quality control review of the audit working papers of the independent auditor who performed the audits for that school district for the prior three fiscal years. If the quality control review of the Controller indicates that the audit was conducted in a manner that may constitute unprofessional conduct as defined pursuant to Section 5100 of the *Business and Professional Code*, including, but not limited to, gross negligence resulting in a material misstatement in the audit, the Controller shall refer the case to the State Board of Accountancy. If the State Board of Accountancy finds that the independent auditor conducted an audit in an unprofessional manner, the independent auditor is prohibited from performing any school district audit for a period of three years, in addition to any other penalties that the State Board of Accountancy may impose.

In addition to EUSD for the fiscal years ended June 30, 1998, 1999, and 2000, the SCO selected additional LEAs for the quality control review: FUSD, NUSD, and the MVROP for the fiscal year ended June 30, 2000.

Objectives, Scope, and Methodology

The general objectives of the quality control review were to determine whether the firm's audits were conducted in compliance with:

- Generally accepted government auditing standards (*Codification of Statements on Auditing Standards Numbers 1-90*, January 2000);
- *Government Auditing Standards*, issued by the Comptroller General of the United States;
- *Standards and Procedures for Audits of California K-12 Local Educational Agencies* (K-12 Audit Guide), published by the SCO; and
- Office of Management Budget (OMB) Circular A-133 and under the provisions of the Single Audit Act.

The following audits performed by the firm were selected for the quality control review:

- Emery Unified School District for the fiscal years ended June 30, 1998, 1999, and 2000
- Fremont Unified School District for the fiscal year ended June 30, 2000
- Newark Unified School District for the fiscal year ended June 30, 2000

In addition, the SCO reviewed the audit working papers for MVROP for the fiscal year ended June 30, 2000. MVROP administers the regional occupational programs for the FUSD and the NUSD. ROP attendance was reported in the attendance records for both of these districts for the fiscal year ended June 30, 2000. The review of the MVROP audit working papers was limited to determining whether the firm complied with the state compliance testing requirements contained in the K-12 Audit Guide.

The quality control review was conducted at the office of Vavrinek, Trine, Day & Co., LLP, in Pleasanton, California. The SCO compared the audit work performed by the firm, as documented in the working papers, with the requirements of the K-12 Audit Guide, federal standards and requirements, and professional auditing standards to determine whether the working papers were adequate to support the audit reports.

Conclusion

The audits referred to above were performed in accordance with some elements of the standards and requirements set forth in GAGAS, GAAS, OMB Circular A-133, and the K-12 Audit Guide; however, many of the auditing standards and requirements were not met. The basis for this opinion is discussed in the Findings and Recommendations section of this report. In addition, the findings by school district are presented in the Summary of Findings by District and Year.

This report is applicable solely to the audit working papers referred to above and is not intended to pertain to any other audit work of the firm.

Views of Responsible Officials

The conclusions reached and review findings were discussed with Linda Todd, partner, at an exit conference on June 18, 2002. It was agreed at the exit conference that a draft report would be issued to the firm's representatives for their response, and it was issued on July 8, 2003.

After receiving the draft report, the firm's representatives requested that the SCO review additional documentation and information related to the findings. Additional information and documentation were provided at a meeting on August 4, 2003, and over the next three months. The findings were modified to reflect the results of the SCO's review and consideration of the additional information and documentation, and a revised draft report was issued to the firm's representatives on April 14, 2004, for their response. Linda Todd responded by the attached letter dated June 14, 2004, disagreeing with the review results.

Restricted Use

This report is intended solely for the information and use of Vavrinek, Trine, Day & Co., LLP (Pleasanton office); the Emery Unified School District; the Fremont Unified School District; the Newark Unified School District; the Mission Valley Regional Occupational Program (MVROP); and the SCO. It is not intended to be and should not be used by anyone other than these specified parties. However, this restriction is not intended to limit distribution of this report, which is a matter of public record.

A handwritten signature in black ink, reading "Jeffrey V. Brownfield". The signature is fluid and cursive, with the first name "Jeffrey" and last name "Brownfield" clearly legible.

JEFFREY V. BROWNFIELD, CPA
Chief, Division of Audits

Findings and Recommendations

General

The Single Audit Act and the *Standards and Procedures for Audits of K-12 Local Educational Agencies* (K-12 Audit Guide), published by the SCO, require audits to be performed in accordance with generally accepted auditing standards (GAAS). These standards deal with the quality of the audits performed by the independent auditor and have been approved and adopted by the American Institute of Certified Public Accountants (AICPA). GAAS is divided into three areas: (1) general standards; (2) fieldwork standards; and (3) reporting standards. The three areas are divided into ten specific standards. In addition to GAAS, auditors of governmental entities must also perform audits in accordance with generally accepted government auditing standards (GAGAS), which expand the GAAS standards in several areas.

In the course of this quality control review, the SCO reviewers found that Vavrinek, Trine, Day & Co., LLP, (VTD) did not comply with many aspects of general, fieldwork, and reporting standards. In addition, VTD did not adequately follow and/or document the testing of the state compliance requirements of the K-12 Audit Guide and the single audit requirements for federal programs.

Finally, VTD did not comply with K-12 Audit Guide requirements for reporting state compliance findings.

Noncompliance with General Standards (GAAS, GAGAS)

FINDING 1— Due professional care deficiencies

VTD did not consistently exercise due professional care in conducting audits and in preparing related reports. Findings 2 through 12 provide examples of the failure to exercise due professional care. Audit reports were not adequately supported by the working papers. The notes to the financial statements were not adequately supported in the working papers. In addition, the working papers did not adequately document the audit procedures that were performed. Also, the audit working papers were difficult to follow because they were not adequately numbered or cross-referenced. This resulted in the additional review by the SCO, and significant discussions with the firm to determine whether audit work performed was sufficient.

Some examples of due professional care deficiencies are as follows:

Based on the SCO review of the EUSD working papers for FY 1998-99 and FY 1999-2000, VTD did not adequately evaluate or test stores inventory.

- In the EUSD FY 1998-99 working papers, there was no documentation supporting stores inventory testing. In the EUSD FY 1999-2000 working papers, inventory balances per the district's records were the same as for FY 1998-99. This may have been an indication that the district did not properly account for FY 1999-2000 activity; however, this was not noted or evaluated by VTD.

- For EUSD FY 1999-2000, general fund materiality was determined to be \$10,700 based on VTD's working papers. General fund stores inventory according to the district's records was \$10,948, which was considered to be material, based on VTD's determination; however, no testing was performed. An auditor's note in the working papers stated, "Client has not performed any inventory procedures . . . since prior year. The records are considered unauditable." However, the reason for the records being considered unauditable was not documented, and no finding or scope limitation was reported.

The EUSD FY 1999-2000 working papers indicated that there was "no payroll clearing" account. However, this was inconsistent with an audit finding included in the report, which was that the district had not performed any bank reconciliations for the payroll clearing account.

The review of the FUSD working papers for FY 1999-2000 disclosed several state compliance deficiencies that indicate a lack of due professional care. For example, for Kindergarten Enrollment, the working papers contained a retention form that was clearly not compliant with *Education Code* requirements; however, VTD did not recognize that the form was deficient, and no finding was reported.

Also, the review of the NUSD working papers for FY 1999-2000 disclosed that testing for attendance accounting was deficient. Although two elementary school sites were selected for testing, the working papers indicated that only one school site was actually tested. There was no explanation or justification as to why only one school site was tested, and VTD management did not note this discrepancy during their review process.

AU Section 339.05 states that working papers:

. . . should be sufficient to show that the applicable standards of fieldwork have been observed. Working papers ordinarily should include documentation showing that—

- a. The work has been adequately planned and supervised. . . .
- b. A sufficient understanding of internal control has been obtained to plan the audit and to determine the nature, timing, and extent of tests to be performed.
- c. The audit evidence obtained, the auditing procedures applied, and the testing performed have provided sufficient competent evidential matter to afford a reasonable basis for an opinion.

AU Section 331.01 states:

Observation of inventories is a generally accepted auditing procedure. The independent auditor who issues an opinion when he has not employed them must bear in mind that he has the burden of justifying the opinion expressed.

AU Section 331.12 states:

When the independent auditor has not satisfied himself as to inventories in the possession of the client through the procedures described in paragraphs .09-.11, tests of the accounting records alone will not be sufficient for him to become satisfied as to quantities; it will always be necessary for the auditor to make, or observe, some physical counts of the inventory and apply appropriate tests of intervening transactions. This should be coupled with inspection of the records of any client's counts and procedures relating to the physical inventory on which the balance-sheet inventory is based.

AU Section 508.22 states:

The auditor can determine that he is able to express an unqualified opinion only if his audit has been conducted in accordance with generally accepted auditing standards and if he has therefore been able to apply all the procedures he considers necessary in the circumstances.

AU Section 508.24 states:

Common restrictions on the scope of the audit include those applying to the observation of physical inventories. . . .

AU Section 326.25 states:

To the extent the auditor remains in substantial doubt about any assertion of material significance, he or she must refrain from forming an opinion until he or she has obtained sufficient competent evidential matter to remove such substantial doubt, or the auditor must express a qualified opinion or a disclaimer of opinion. . . .

GAGAS 3.26 states:

Due professional care should be used in conducting the audit and in preparing related reports.

GAGAS 3.28 states:

Exercising due professional care means using sound judgement in establishing the scope, selecting the methodology, and choosing tests and procedures for the audit. The same sound judgement should be applied in conducting the tests and procedures and in evaluating and reporting the audit results.

GAGAS 3.29 states:

Auditors should use sound professional judgement in determining the standards that apply to the work to be conducted. The auditors' determination that certain standards do not apply to the audit should be documented in the working papers. . . .

Recommendation

VTD should comply with GAAS and GAGAS in performing audits.

VTD should ensure that audit reports are adequately supported by the working papers. In addition, the working papers should include all audit procedures performed, and working papers should be adequately numbered and cross-referenced.

Also, VTD should ensure that it reports all findings and scope limitations in the audit report. Furthermore, VTD should ensure that it audits all material amounts, thoroughly documents why a material amount was not audited, or performs and documents alternative audit procedures.

Firm's Response

The firm disagrees with the finding. However, the firm disputes some specific examples provided as support to the finding and agrees with others (see Attachment 1, pages 1-3, for detail).

SCO's Comment

The finding remains unchanged (see Attachment 2, page 1).

Noncompliance with *Generally Accepted Government Auditing Standards* (GAGAS)

FINDING 2— Quality control deficiencies

Reviews of work performed were not consistently completed or documented in the working papers. This is also in violation of VTD's established policy for review of staff work.

For EUSD FY 1997-98, there was no indication of an overall working paper review or review of the auditor's reports by the manager, supervisor, or partner. In addition, there was no indication of a second-level overall review of the working papers or the auditor's reports by an independent partner. Also, the partner signing the auditor's reports did not sign VTD's review and approval form.

In addition, all audit files except for MVROP had quality control deficiencies. For example, there was no evidence of supervisory review on most of the internal control surveys and audit programs, including revolving fund cash, student body funds, investments, single audit master program, payroll, and inventory.

GAGAS 3.31 states:

Each audit organization conducting audits in accordance with these standards should have an appropriate internal quality control system in place. . . .

GAGAS 3.32 states:

The internal quality control system established by the audit organization should provide reasonable assurance that it (1) has adopted, and is following, applicable auditing standards and (2) has established, and is following, adequate audit policies and procedures. . . .

VTD's established policy is that key audit areas—including planning documentation, audit programs, the understanding and testing of internal control, and legal and client representation letters—be reviewed and signed off by the engagement partner.

If the firm spent sufficient time and care in reviewing working papers, many of the findings presented throughout this report might have been identified and corrected during the review process. For example, during the review process, the firm should have identified and corrected documentation deficiencies, lack of adequate follow up on potential audit findings, and state and federal compliance testing and sampling deficiencies.

Recommendation

VTD should comply with auditing standards and its own policy to ensure that staff work is adequately reviewed and that the review is documented in the working papers.

Firm's Response

The firm disagrees with the finding. However, the firm agrees in part with the finding regarding EUSD for FY 1997-98 (see Attachment 1, page 3, for detail).

SCO's Comment

The finding remains unchanged (see Attachment 2, page 1).

Noncompliance with Fieldwork Standards for Financial Audits (GAAS)

FINDING 3— Analytical review deficiencies in planning

VTD did not consistently document analytical review procedures in planning the audits. Therefore, the SCO reviewers were unable to determine if the procedures were adequate and in compliance with professional standards.

For example, in EUSD's working papers for FY 1997-98 and FY 1998-99, and NUSD's working papers for FY 1999-2000, there was no documentation of analytical review procedures with regard to planning.

AU Section 329.04 states:

Analytical procedures should be applied to some extent for the purposes referred to in . . . [(a) To assist the auditor in planning the nature, timing, and extent of other auditing procedures] for all audits of financial statements made in accordance with generally accepted auditing standards.

AU Section 329.06 states:

The purpose of applying analytical procedures in planning the audit is to assist in planning the nature, timing and extent of auditing procedures that will be used to obtain evidential matter for specific account balances or classes of transactions.

Unusual transactions or events, accounting changes, or misstatements may not be identified if analytical procedures are not performed in the planning phase of the audit.

Recommendation

VTD should ensure that it consistently applies analytical procedures in planning audits. In addition, VTD should ensure that the results and conclusions are adequately documented in the working papers.

Firm's Response

The firm disagrees with the finding (see Attachment 1, pages 3-4, for detail).

SCO's Comment

The finding remains unchanged (see Attachment 2, page 1).

FINDING 4— Deficiencies in consideration of computer processing system in planning

VTD did not document the effect of the district computer processing system on the audits. For example, in the EUSD FY 1998-99 working papers, there was no documentation to support VTD's consideration of the effect of computer processing by the district.

For EUSD in FY 1999-2000, the firm's consideration of computer processing related only to the attendance process.

In addition, VTD did not document its consideration and evaluation of the Alameda County Office of Education's (ACOE) computer processing on any of the districts reviewed. The ACOE provided services to the various districts that were part of the districts' information systems. VTD did not evaluate or document the effect of ACOE's services on the districts' internal control in planning the audit, or in assessing control risk.

AU Sections 324.03 to 324.21 provide guidance to auditors regarding their consideration of the effect of the service organization on the user organization's internal control and the availability of audit evidence.

AU Section 311.09 states:

The auditor should consider the methods the entity uses to process accounting information in planning the audit because such methods influence the design of internal control. The extent to which computer processing is used in significant accounting applications, as well as the complexity of that processing, may also influence the nature, timing and extent of audit procedures.

GAGAS requires additional documentation in Section 4.21.3 as follows:

The additional internal control standard for financial statement audits is

In planning the audit, auditors should document in the working papers (1) the basis for assessing control risk at the maximum level for assertions related to material account balances, transaction classes, and disclosure components of financial statements when such assertions are significantly dependent upon computerized information systems, and (2) consideration that the planned audit procedures are designed to achieve audit objectives and to reduce audit risk to an acceptable level.

Section 4.21.4 states:

This additional GAGAS standard does not increase the auditor's responsibility for testing controls, but rather requires that, if the auditor assesses control risk at the maximum level for assertions related to material account balances, transaction classes, and disclosure components of financial statements when such assertions are significantly dependent upon computerized information systems, the auditor should document in the working papers . . . the basis for that conclusion by addressing (1) the ineffectiveness of the design and/or operation of the controls, or (2) the reasons why it would be inefficient to test the controls. In such circumstances, GAGAS also require the auditor to document in the working papers the consideration that the planned audit procedures are designed to achieve specific audit objectives and, accordingly, to reduce audit risk to an acceptable level. This documentation should address:

- a. the rationale for determining the nature, timing, and extent of planned audit procedures;
- b. the kinds and competence of available evidential matter produced outside a computerized information system; and
- c. the effect on the audit opinion or report if evidential matter to be gathered during the audit does not afford a reasonable basis for the auditor's opinion on the financial statements.

If the district computer processing system is not evaluated during the planning stage of the audit, the evaluation of internal control may not be accurate, and planned audit tests may not be adequate.

Recommendation

VTD should ensure that it evaluates and documents the effect of the district's computer processing system on the audit.

Firm's Response

The firm agrees with the finding (see Attachment 1, page 4, for detail).

SCO's Comment

The finding remains unchanged (see Attachment 2, page 2).

**FINDING 5—
Internal control
deficiencies**

VTD did not adequately document its understanding of district policies and procedures in relation to the control environment, accounting system, and control procedures. In addition, VTD did not consistently determine whether internal control policies and procedures had been placed in operation. Also, VTD always assessed control risk at the maximum level.

VTD did not document control risk for the assertions embodied in the account balance, transaction class, and disclosure components of the financial statements as required by SAS 78, which was effective for audits of financial statements for periods beginning on or after January 1, 1997.

VTD representatives explained that the firm's standard procedure was to perform a walk-through to better understand the internal control system. However, the SCO reviewers noted several instances where discrepancies were identified during the walk-through, but these were not evaluated, nor was an internal control finding reported. The following are some examples of the discrepancies.

In the EUSD FY 1997-98 working papers, VTD did not clearly document its understanding of the design of policies and procedures for internal control. In addition, VTD's determination of whether policies and procedures had been placed in operation was limited to discussions with district staff and the results of a walk-through.

The following deficiencies were noted. In testing cash disbursement transactions, two of three invoices tested did not have receiving documents or signatures. In addition, one of three invoices tested was not stamped as paid, and it appears that the amounts were not traced to the general ledger. However, the auditor concluded that cash disbursement procedures appeared to be adequate. No internal control findings were reported for any of these exceptions.

In the EUSD FY 1998-99 working papers for walk-through of disbursements, exceptions were noted for three of six transactions; however, no conclusion regarding disbursement internal controls was documented and no internal control finding was reported.

Deficiencies were noted on several of the internal control questionnaires. Some examples are as follows:

- Organization and Personnel Practices: Several questions were answered “No”; however, there was no auditor comment, explanation, or discussion. Also, some questions were not answered.
- Internal Control Survey, Payroll: Several questions were answered “No”; however, there was no auditor comment or explanation.

AICPA standards and GAGAS require that auditors obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

AU Section 319.01 states:

A sufficient understanding of internal control is to be obtained to plan the audit and to determine the nature, timing, and extent of tests to be performed.

AU Section 319.02 states:

In all audits, the auditor should obtain an understanding of internal control sufficient to plan the audit by performing procedures to understand the design of controls relevant to an audit of financial statements, and whether they have been placed in operation.

AU Section 319.03 states:

After obtaining this understanding, the auditor assesses control risk for the assertions embodied in the account balance, transaction class, and disclosure components of the financial statements. The auditor may assess control risk at the maximum level (the greatest probability that a material misstatement that could occur in an assertion will not be prevented or detected on a timely basis by an entity’s internal control) because he or she believes controls are unlikely to pertain to an assertion, are unlikely to be effective, or because evaluating their effectiveness would be inefficient.

AU Section 319.05 states:

The auditor uses the knowledge provided by the understanding of internal control and the assessed level of control risk in determining the nature, timing and extent of substantive tests for financial statement assertions.

AU Section 319.44 states:

The auditor should document the understanding of the entity’s internal control components obtained to plan the audit. The form and extent of this documentation is influenced by the size and complexity of the entity, as well as the nature of the entity’s internal control.

AU Section 319.57 states:

In addition to the documentation of the understanding of internal control . . . the auditor should document the basis for his or her conclusions about the assessed level of control risk.

GAGAS discusses controls over compliance with laws and regulations. Section 4.30 states:

AICPA Standards and GAGAS require auditors to design the audit to provide reasonable assurance that the financial statements are free from material misstatements resulting from violations of laws and regulations that have a direct and material effect on the determination of financial statement amounts. To meet that requirement, auditors should have an understanding of internal controls relevant to financial statement assertions affected by those laws and regulations. Auditors should use that understanding to identify types of potential misstatements, consider factors that affect the risk of material misstatement, and design substantive tests.

If internal controls are not adequately evaluated, including proper consideration of exceptions noted during walk-throughs, internal control weaknesses may not be identified. If control risk is not properly evaluated, substantive tests may not be appropriately or adequately designed, and errors may not be detected.

Recommendation

VTD should ensure that it adequately documents its understanding of the control environment, and policies and procedures for the control environment, accounting system, and control procedures. In addition, VTD should consistently determine and document whether internal control policies and procedures had been placed in operation. Also, VTD should ensure that it assesses and documents control risk for the assertions embodied in the account balance, transaction class, and disclosure components of the financial statements. Furthermore, VTD should adequately evaluate exceptions noted during walk-throughs and consider expanding testing or reporting an internal control finding.

Firm's Response

The firm disagrees with the finding (see Attachment 1, pages 4-5, for detail).

SCO's Comment

The finding remains unchanged (see Attachment 2, page 2).

FINDING 6— Working paper deficiencies

There were numerous working paper deficiencies for each LEA audit reviewed. In general, the working papers did not provide adequate support for the work performed and the conclusions reached during the audit. Many exceptions were noted in the financial working paper documentation. For example, the financial statement amounts did not consistently trace to lead sheet amounts or supporting documentation, and working papers did not consistently contain the objectives, scope, and methodology, documentation of the work performed, and evidence of supervisory reviews.

In the EUSD FY 1997-98 working papers, the following deficiencies were noted:

- For accounts payable, according to the working papers, two adjusting entries should have been made; however, there was no explanation provided and no indication whether they were actually made.
- For accounts payable Building Fund accruals, one item out of a population of three was selected for testing; however, no testing was actually performed because it was considered to be an immaterial amount (\$8,723.87 out of \$14,233.56). It is not reasonable to select an item for testing and then not test it because it is considered to be immaterial.

In the EUSD FY 1998-99 working papers, the accounts payable leadsheet contained an item referenced to a worksheet with no indication of the source of any of the numbers contained in it, and there was no other supporting documentation. In addition, the deferred revenue documentation consisted of a worksheet that was referenced to the J-200 and J-390 reports, which are unaudited amounts. The worksheet indicated that selected items were verified through programs; however, there was no other supporting documentation.

In the FUSD FY 1999-2000 working papers, the following discrepancies were noted for specific account balances, as follows:

- Cash and Investments: The amount presented in the financial statements was \$1,075,855 more than the amount documented in the working papers. No explanation for the discrepancy was noted.
- Accounts Payable–Total Liability: The amount presented in the financial statements was \$1,287,883 more than the amount documented in the working papers. No explanation for the discrepancy was noted.

In the NUSD FY 1999-2000 working papers, the following deficiencies were noted:

- The amounts presented for fund balances and general long-term debt in the notes to the financial statements were not supported by the working papers. For general long-term debt, the amounts presented in the working papers did not agree with the amounts reported.
- Revenues and expenditures presented in the financial statements did not agree with or were not supported by the working papers.
- For deferred revenue, the reported amounts agreed to a worksheet supported by the J-200 and J-390 reports, which are unaudited amounts. In addition, the working papers indicated that the amounts were verified through programs; however, no supporting documentation was found.

AU Section 339.01 states:

The auditor should prepare and maintain working papers, the form and content of which should be designed to meet the circumstances of a particular engagement. The information contained in the working papers constitutes the principal record of the work that the auditor has done and the conclusions that he has reached concerning significant matters.

AU Section 339.02 states:

Working papers serve mainly to—
a. Provide the principal support for the auditor's report, including his representation regarding observations of the standards of field work, which is implicit in the reference in his report to generally accepted auditing standards.
b. Aid the auditor in the conduct and supervision of the audit.

AU Section 339.05 states:

In addition, working papers "should be sufficient to show that the applicable standards of fieldwork have been observed. Working papers ordinarily should include documentation showing that—

- a. The work has been adequately planned and supervised, indicating observance of the first standard of fieldwork.
- b. A sufficient understanding of internal control has been obtained to plan the audit and to determine the nature, timing, and extent of tests to be performed.
- c. The audit evidence obtained, the auditing procedures applied, and the testing performed have provided sufficient competent evidential matter to afford a reasonable basis for an opinion.

GAGAS 4.35 states:

The additional working paper standard for financial statement audits is: Working papers should contain sufficient information to enable an experienced auditor having no previous connection with the audit to ascertain from them the evidence that supports the auditors' significant conclusions and judgements.

GAGAS 4.37 states:

Working papers should contain

- a. the objectives, scope, and methodology, including any sampling criteria used;
- b. documentation of the work performed to support significant conclusions and judgments, including descriptions of transactions and records examined that would enable an experienced auditor to examine the same transactions and records, and
- c. evidence of supervisory reviews of the work performed.

Without adequate documentation, the judgments made and conclusions reached may not be accurate or valid.

Recommendation

VTD should ensure that working papers are prepared in accordance with GAGAS and GAAS.

Firm's Response

The firm disagrees with the finding. However, the firm agrees with specific examples provided as support for the finding (see Attachment 1, pages 5-7, for detail).

SCO's Comment

The finding remains unchanged (see Attachment 2, pages 2-4).

**FINDING 7—
Deficiencies in
evaluating fraud,
illegal acts, and other
noncompliance**

VTD did not adequately address potential fraud, illegal acts, or other noncompliance during the EUSD FY 1998-99 audit.

For example, the working papers noted that “Dr. Handy, Supt. and Gina Peters are key people at the district, small staff limits segregation duties. District has management oversight.” However, VTD did not adequately evaluate or document the potential for indirect illegal acts to occur, and did not apply audit procedures to ascertain whether fraud, illegal acts, or other noncompliance had occurred.

In addition, the working papers indicate that the district had a conflict of interest policy; however, there was no indication that the policy was reviewed or evaluated.

Also, there were several inconsistencies in responses to the evaluation and planning form questionnaire related to conflict of interest and related party transactions. For example, VTD's responses were changed from “yes” to “no”; however, there was no indication who revised the responses, or why.

At the end of the evaluation and planning form, VTD noted that “no modifications are planned, if modifications are warranted, they will be indicated on individual workpapers.” However, no modification of any individual working papers was noted during the review.

GAGAS 4.12 c states:

Auditors should be aware of the possibility that indirect illegal acts may have occurred. If specific information comes to the auditors' attention that provides evidence concerning the existence of possible illegal acts that could have a material effect on the financial statements, the auditors should apply audit procedures specifically directed to ascertaining whether an illegal act has occurred.

GAGAS 4.13 states:

Auditors should design the audit to provide reasonable assurance of detecting material misstatements resulting from noncompliance with provisions of contracts or grant agreements that have a direct or material effect on the determination of financial statement amounts. If specific information comes to the auditors' attention that provides evidence concerning the existence of possible noncompliance that could have a material indirect effect on the financial statements, auditors should apply audit procedures specifically directed at ascertaining whether that noncompliance has occurred.

Because potential fraud, illegal acts, and other noncompliance were not adequately addressed, errors and irregularities that may have had a material effect on the financial statements may not have been identified.

Recommendation

VTD should ensure that it adequately addresses potential fraud, illegal acts, or other noncompliance when conducting audits. If potential fraud, illegal acts, or other noncompliance are identified, VTD should evaluate the possibility and design, apply, and document the audit procedures specifically directed at ascertaining whether illegal acts or noncompliance have occurred.

Firm's Response

The firm disagrees with the finding (see Attachment 1, page 7, for detail).

SCO's Comment

The finding remains unchanged (see Attachment 2, page 4).

**FINDING 8—
Reporting
deficiencies**

In its reports, VTD stated the LEA audits were performed in accordance with generally accepted auditing standards, government auditing standards, and the K-12 Audit Guide. In addition, in the audit report on major programs, VTD incorrectly stated that it performed its audits in accordance with the standards contained in OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

Because VTD did not comply with all applicable standards as evidenced by all of the findings in this report, the independent auditor's report, the independent auditor's report on compliance and on internal control over financial reporting, the independent auditor's report on compliance with requirements applicable to each major program and internal control over compliance, and the independent auditor's report on state compliance are incorrect.

Findings 1 through 7 identify GAAS and GAGAS deficiencies which substantiate that VTD did not perform the audits in accordance with all applicable standards.

Findings 9 and 10 identify state compliance deficiencies which substantiate that VTD did not perform the audits in accordance with the GAGAS and the K-12 Audit Guide.

Findings 11 and 12 identify federal internal control and compliance deficiencies which substantiate that VTD did not perform the audits in accordance with OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

GAGAS 5.11 states:

Audit reports should state that the audit was made in accordance with generally accepted governmental auditing standards.

GAGAS 5.12 states:

The above statement refers to all the applicable standards that the auditors should have followed during their audit. The statement should be qualified in situations where the auditors did not follow an applicable standard. In these situations, the auditors should disclose the applicable standard that was not followed, the reasons therefor, and how not following the standard affected the results of the audit.

If all applicable standards are not followed, and the audit reports are not modified to reflect this, the reports may be misleading, and the effect on the results of the audit will not be adequately disclosed.

Recommendation

VTD should follow all applicable standards when performing audits. If applicable standards are not followed, the audit reports should be modified to disclose the standards that were not followed, the reasons, and effect on the results of the audit.

Firm's Response

The firm disagrees with the finding (see Attachment 1, pages 7-8, for detail).

SCO's Comment

The finding remains unchanged (see Attachment 2, page 4).

Noncompliance With K-12 Audit Guide Requirements

FINDING 9— State compliance testing and reporting deficiencies

VTD did not consistently perform the state compliance audit procedures in the K-12 Audit Guide for each of the audits reviewed, or document the reason why procedures were not performed. In addition, some procedures performed were not adequately documented, or were incomplete or inaccurate. Also, some findings that should have been reported were not.

For the EUSD FY 1997-98 audit, for the staff development days program, three procedures were included in the K-12 Audit Guide; however, according to the audit program, the VTD auditor only tested to determine if staff development days appeared on the district calendar. No other documentation or testing was noted. The report on state compliance was not modified, as required.

For the EUSD FY 1998-99 audit, several state compliance testing deficiencies were noted, as follows:

- **Kindergarten Enrollment:** The K-12 Audit Guide requires the auditor to “Select a representative sample of kindergarten pupils from the district’s attendance records. . . .” However, no testing was performed because the site selected for testing was a high school, and there were no kindergarten pupils at the high school. However, the audit report stated that all four audit procedures were performed.
- **Staff Development Days:** Limited testing appears to have been performed. VTD did not examine contemporaneous documents to determine the validity of the claim for reimbursement of instructional time and staff development reform program days. In addition, staff development days identified by VTD did not agree to district records. There was no explanation in the working papers and state compliance report for why the audit procedures were not performed, and no finding was reported.
- **Class Size Reduction Program:** The testing period did not cover the required period. VTD tested the period of September 9 to December 16; however, the required period should have been September 10 to April 15. As a result, testing included a day prior to the start of the school year, and excluded the period from December 17 to April 15. Therefore, the average class sizes required to be calculated may have been inaccurate. In addition, the working papers noted an amount was not included in the class size reduction calculation and that the district would be making a revision; however, there was no indication that this was actually done. No finding was included in the audit report.

In addition, VTD did not consistently apply the audit procedures for testing attendance. The working papers indicated that the internal control survey for attendance was in the system file. However, VTD did not provide SCO reviewers with an internal control survey for FY 1998-99. Also, none of the prior internal control surveys in the system file had been updated, nor was there any indication of review for FY 1998-99. The working papers indicated that one document was tested for accuracy by cross-footing; however, the SCO reviewers identified an error on the document that had not been detected by VTD.

For the EUSD FY 1999-2000 audit for incentives for longer instructional day, based on the SCO review of the working papers, kindergarten instructional minutes offered equaled 200 minutes for both the morning and afternoon sessions. However, according to the audit report, there were 210 minutes for each session. Consequently, the schedule of instructional time included in the audit report was incorrect.

For the FUSD FY 1999-2000 audit, the SCO reviewers noted several deficiencies in state compliance testing. For example, the staff development day program was not properly tested as the firm did not correctly apply the suggested audit procedures. The firm selected eight schools to test; however, when non-compliance was noted it was not

recognized as an audit finding and not reported. In addition, the working papers showed that two of the staff development days for Chadbourne Elementary were “undecided” in terms of the topic. The related funding for these two days should have been disallowed because of the undecided nature of the staff development days. Hirsch Elementary was also selected for testing. The purposes for the three staff development days were Back to School Night, Winter Party, and Valentine’s Party. All three staff development days and the related funding should have been disallowed. In addition, for Hirsch Elementary, there is a notation that “Per ICQ and inquiry, all SDD are on minimum days and are taking place after the students left school. No further testing will be needed.”

The working papers also showed that the staff development days for Glenmoor Elementary, Weibel Elementary and Walters Jr. High were selected for testing. The testing working papers contained the comment “See system file for SDD of the whole district.” The system file did not contain any discussion of staff development days for these school sites.

The report on state compliance was not modified to reflect the actual number of procedures performed. Instead, the report on state compliance indicated that all required procedures were performed.

In addition, for the state instructional materials fund, the audit procedure in the K-12 Audit Guide requires the auditor to determine if the FUSD posted a ten-day notice of the hearing. The working papers indicated that the district did not comply with this requirement, as there was only a two-day notice. However, no finding was reported.

For the NUSD FY 1999-2000 audit, Class Size Reduction (Option One): There was no evidence that the auditor performed the required procedures to determine the average daily class size for specified sample classes. However, the report on state compliance reflected that all 12 procedures were performed.

Morgan Hart (Grade 9) Class Size Reduction: The working papers indicated that there was a finding regarding the district not having documents to support the claim for Morgan Hart funds. It appears that the district overclaimed three FYE. However, this was not reported as an audit finding and there was no indication of the disposition of the finding.

For the Mission Valley ROP FY 1999-2000 audit, the report on state compliance stated that all four procedures related to attendance reporting were performed. However, the SCO’s review disclosed that the following procedures were not performed:

- Audit procedure 3a requires the auditor to reconcile the monthly totals on the site’s attendance summary to the summary maintained by the LEA for the annual attendance reports. However, there was insufficient evidence in the working papers to support that this step was performed.

- Audit procedure 3c requires the auditor to select a representative sample of classes (teachers) and trace the monthly totals from the monthly report to the attendance registers, scantron summaries, etc. However, there was no evidence in the working papers to support that this step was performed.
- Audit procedure 4 requires the auditor to select a sample of excused absence documentation (notes, logs, etc.) and compare to documentation supporting ADA reported to the State to verify that excused absences were not claimed for apportionment. However, there was no evidence in the working papers to support that this procedure was performed.

There were no explanations in the working papers or in the report on state compliance regarding why the procedures were not performed, or if alternative procedures were applied.

The K-12 Audit Guide, Section 510, states:

All state requirements identified in Section 520 that are applicable to the entity must be tested for compliance with state laws and regulations . . . [In addition,] Each compliance requirement is accompanied by suggested audit procedures that can be utilized as determined by the auditor's professional judgement.

GAGAS 4.34 states:

AICPA standards and GAGAS require the following: A record of the auditors' work should be retained in the form of working papers.

GAGAS 4.35 states:

The additional working paper standard for financial statement audits is: Working papers should contain sufficient information to enable an experienced auditor having no previous connection with the audit to ascertain from them the evidence that supports the auditors' significant conclusions and judgments.

GAGAS 5.15 regarding reporting compliance with laws and regulations, states:

In presenting the results of those tests [compliance with laws and regulations] auditors should report fraud, illegal acts, or other material noncompliance. . . .

Education Code 14503(a) states:

For each state program compliance requirement included in the audit guide, every audit report shall further state that the suggested audit procedures included in the audit guide for that requirement were followed in the making of the audit, if that is the case, or, if not, what other procedures were followed.

If state compliance procedures are not performed adequately and accurately, illegal acts or other noncompliance may not be detected, and the report on state compliance may be incorrect.

Recommendation

VTD should ensure that the state compliance audit procedures are performed with sufficient attention toward complying with the K-12 Audit Guide. Sufficient resources should be allocated toward compliance areas to ensure that relevant procedures are properly completed and any noncompliance is properly reported. The firm should modify the report as required to disclose the actual procedures performed.

Firm's Response

The firm agrees with some of the items noted; however, the firm disagrees with others (see Attachment 1, pages 8-9, for detail).

SCO's Comment

The finding remains unchanged (see Attachment 2, pages 4-6).

**FINDING 10—
State compliance
sample selection
deficiencies and
expansion of testing**

Sampling methodology for state compliance testing was not adequate. The K-12 Audit Guide requires that representative samples be selected for testing. In addition, GAGAS Section 4.37 requires that working papers contain any sampling criteria used. The universe of transactions was not identified and sampling criteria was not consistently documented in the working papers. Also, when exceptions were noted, sampling was not expanded and findings were not consistently reported.

The following are some examples:

- In the EUSD FY 1997-98 working papers for excused absence testing, eight students were selected from month six; however, no population or universe was stated. In addition, for state instructional materials testing, the working papers indicated that exceptions were noted in two of three items tested; however, testing was not expanded nor was a finding reported.
- For EUSD for FY 1998-99, State Instructional Materials Fund testing, four transactions were selected for testing. The universe of transactions was not identified and the sampling methodology was not documented. In addition, one exception was noted; however, testing was not expanded nor was a finding reported. Instead, the VTD auditor concluded, "Appears to be in compliance."
- For EUSD for FY 1999-2000, Excused Absences; five students were selected for testing; however, the population was not identified. One exception was noted; however, the VTD auditor noted that it "appears to be an isolated incident." Testing was not expanded, nor was a finding reported.
- For FUSD for FY 1999-2000, Incentive for Longer Instructional Days: seven schools out of 41 were selected for testing; however, the working papers did not indicate how the schools or number of schools were selected or the sampling methodology used.

- For NUSD for FY 1999-2000, Kindergarten Enrollment; three pupils out of a population of approximately 505 kindergartners were selected for testing, which was approximately .006% of the population. The audit guide requires the auditor to select a representative sample for testing.

GAGAS 4.37 states, in part:

Working papers should contain (a) the objectives, scope, and methodology, including any sampling criteria used.

The K-12 Audit Guide discusses expanding sample size in Section 336 as follows:

It is inadequate for the auditor to solely identify and report exceptions without determining if further testing is needed or if the auditee should review or reconstruct relevant records and quantify the related fiscal impact. Determining how to proceed requires significant auditor evaluation and judgment.

If exceptions are discovered when performing tests, the auditor should assess and evaluate the exception rate and type to determine if the sample should be expanded and additional testing be performed. The sample should be representative of the population and sufficient in size to allow the auditor to draw a reasonable conclusion.

For example, if testing a sample of 100 items results in 10 exceptions, or a 10% exception rate, the auditor should expand the sample and perform further testing. If the auditor determines that the exceptions are the result of a systemic problem, the auditor may:

1. Use a statistically valid sampling methodology to extrapolate the results of the tests over the entire population and quantify the fiscal impact, or,
2. Require the auditee to review or reconstruct all of the relevant records and quantify the related fiscal impact. The auditor should then perform testing to determine the reasonableness of the results of the auditee's work.

However, if the auditor determines that the exception is due to an isolated cause, the auditor may deem further audit work unnecessary. (Refer to SAS 39-Audit Sampling for further guidance.)

If sample sizes are not properly selected or evaluated, the sizes may not be representative of the population, the conclusions reached may not be accurate, and the auditor's opinion in the report on state compliance may be incorrect. Professional judgment would dictate that when exceptions are noted, the sample should be expanded.

Recommendation

VTD should ensure that it complies with GAGAS standards and the K-12 Audit Guide requirements when selecting and evaluating samples.

Firm's Response

The firm agrees, in part, with the finding (see Attachment 1, page 9, for detail).

SCO's Comment

The finding remains unchanged (see Attachment 2, page 6).

Noncompliance With Federal Single Audit Requirements

FINDING 11— Federal program internal control deficiencies

VTD did not comply with federal requirements regarding the evaluation and testing of internal control over compliance for federal programs. The working papers reviewed did not adequately document whether VTD performed procedures to obtain an understanding of internal control over compliance that is sufficient to support a low assessed level of control risk for major programs. Instead, VTD relied on its evaluation of internal controls over the financial statements, which was limited to walk-throughs. When the walk-through resulted in a deviation from the documented control, VTD did nothing to address the deviation (see Finding 5 for more discussion). VTD consistently assessed the internal control risk at maximum and did not perform tests of controls. In addition, VTD did not plan the testing of internal control over compliance for major programs to support a low assessed level of control risk for the assertions relevant to the compliance requirements for each major program. Also, the federal internal control testing performed was not adequately documented.

For example, in the EUSD FY 1999-2000 working papers, the single audit control risk was assessed at low, based on the results of a questionnaire. However, there were two findings and recommendations related to federal program internal control deficiencies from the prior year's audit, one of which had not been implemented. In addition, fraud allegations had been made against the former superintendent. This would not support a low-risk assessment.

In the NUSD FY 1999-2000 working papers, the review of federal program internal control was based on internal control questionnaires in the general evaluation and planning questionnaire. Specific support for federal internal controls was not evident in the working papers. The planning federal programs questionnaire was designed to cover multiple years. There was no specific reference to the year being audited.

OMB Circular A-133, Section .500, requires the auditor to:

1. Perform procedures to obtain an understanding of internal control over compliance for federal programs that is sufficient to plan the audit to support a low assessed level of control risk for major programs.
2. Plan the testing of internal control over major programs to support a low assessed level of control risk for the assertions relevant to the compliance requirements for each major program.
3. Perform testing of internal control.

Inadequate testing of internal control over compliance for major federal programs may result in internal control weaknesses or reportable conditions not being identified. In addition, without adequate testing of internal controls, the opinion expressed in the auditor's report on compliance with internal controls over compliance for federal programs may not be accurate.

Recommendation

VTD should comply with the requirements of OMB Circular A-133 regarding testing internal control over compliance for federal programs.

Firm's Response

The firm disagrees with the finding. However, the firm agrees with a specific finding regarding EUSD for FY 1999-2000 (see Attachment 1, page 10, for detail).

SCO's Comment

The finding remains unchanged (see Attachment 2, pages 6-7).

FINDING 12— Federal program compliance deficiencies

VTD tested only Type A federal programs. VTD did not identify or test low-risk Type A programs or high-risk Type B programs. Type A programs are generally federal programs with more than \$300,000 in total federal expenditures. Any federal programs that do not meet the Type A criteria are considered Type B programs. In addition, VTD did not consistently review all 14 types of compliance requirements. The firm stated that its approach was that these compliance requirements were not applicable for any local educational agencies. Therefore, it was not considered whether these requirements should be treated on an LEA by LEA basis. VTD frequently noted in the working papers that certain compliance requirements were not applicable, but no explanation was provided. Written audit procedures were often not performed, and the procedures performed were not adequately documented in the working papers.

For example, in the EUSD FY 1998-99 and FY 1999-2000, FUSD FY 1999-2000, and NUSD FY 1999-2000 working papers for federal compliance testing, the components required to be tested by OMB Circular A-133 were marked as "N/A" by the firm; however, no explanations were provided.

The firm's audit program noted that several federal compliance requirements applicable to the Child Nutrition Cluster (School Breakfast Program (10.553) and National School Lunch Program (10.555)) according to the OMB Circular A-133 Compliance Supplement were "N/A" (not applicable); however, there was no explanation for why these compliance requirements did not apply.

The components marked as “N/A” included the following:

- Cash management
- Equipment and real property management
- Program income
- Reporting
- Subrecipient monitoring
- Procurement and suspension and debarment (NUSD only)

In addition, in the NUSD FY 1999-2000 audit report, there was a federal program finding regarding multi-funded position reporting deficiencies; however, the working papers did not contain any reference to this finding. No exceptions for federal programs were noted in the working papers.

OMB Circular A-133, Section .520, describes the requirements related to major program determination by the auditor. This section requires that, in addition to Type A programs, the auditor should identify low-risk Type A programs and Type B programs. Also, the auditor should document in the working papers the risk analysis process used in determining major programs.

OMB Circular A-133 further states that compliance testing shall include tests of transactions and such other auditing procedures necessary to provide the auditor with sufficient evidence to support an opinion on compliance.

The OMB Circular A-133 Compliance Supplement, defines 14 types of compliance requirements and the related audit objectives that the auditor shall consider in every audit. Suggested audit procedures are also provided to assist the auditor.

Without adequate testing, deficiencies may not have been identified or reported. In addition, the opinion expressed in the auditor’s report on compliance for major federal programs may not be accurate.

Recommendation

VTD should comply with the requirements of OMB Circular A-133 with regard to testing federal programs. In addition, VTD should consider all federal compliance requirements for testing on an LEA by LEA basis. If certain requirements are not applicable, VTD should document the explanation.

Firm’s Response

The firm disagrees with the finding (see Attachment 1, pages 10-12, for detail).

SCO’s Comment

The finding remains unchanged (see Attachment 2, page 7).

Summary of Findings by District and Year

General

The following findings represent the results of the SCO's review of the working papers by district and year of the audit.

The findings presented in the following summary correspond to the findings presented in the overall Findings and Recommendation Section of this report. The overall findings do not necessarily pertain to each district and year reviewed; therefore, only those applicable to each district and year are included.

Emery Unified School District, Fiscal Year 1997-98

FINDING 1— Due professional care deficiencies

The source for several of the amounts and information presented in the financial statements was unclear. When indicated, amounts presented were supported by the J-200 report which are unaudited amounts. In addition, usually the J-200 was not supported by other documentation. Also, in some instances the working papers were not adequately numbered or cross-referenced.

Findings 9 and 10 also contain examples of due professional care deficiencies.

FINDING 2— Quality control deficiencies

There was no indication of an overall working paper review or review of the auditor's reports by the manager, supervisor, or partner. In addition, there was no indication of a second-level overall review of the working papers or the auditor's reports by an independent partner. Also, the partner signing the auditor's reports did not sign VTD's review and approval form.

There was usually no indication of supervisory review on working papers prepared by assistants, although in many cases a line was provided for signature and date. For example:

- Internal control—General long-term debt
- Audit program for cash
- Cash lead sheet
- Equipment inventory audit program
- Student body funds
- General procedures
- Investments
- Accounts receivable

In addition, the many state compliance deficiencies indicate poor quality control (see Finding 9).

**FINDING 3—
Analytical review
deficiencies in planning**

Analytical review procedures appeared to be limited to a comparison of budget versus actual amounts performed at the end of the audit. In addition, there was not sufficient detail or documentation to indicate if analytical review procedures were used to assist in planning the nature, timing, and extent of other auditing procedures.

**FINDING 5—
Internal control
deficiencies**

The working papers did not indicate if the firm assessed control risk for the assertions embodied in the account balance, transaction class, and disclosure components of the financial statements as required by SAS 78, which was effective for audits of financial statements for periods beginning on or after January 1, 1997.

In addition, several deficiencies were noted, as follows:

- In testing cash disbursement transactions, two of three invoices tested did not have receiving documents or signatures. In addition, one of three invoices tested was not stamped as paid, and it appears that the amounts were not traced to the general ledger. However, the auditor concluded that cash disbursement procedures appeared to be adequate. No internal control findings were reported.
- In testing of classified payroll, out of six employees tested, one I-9 form was missing. The missing form was determined to be an isolated instance and testing was not expanded, nor was a finding reported. For another employee tested, there was a notation, "Awaiting a letter from Gina." However, no further explanation was provided nor was there any indication that any follow up occurred. In addition, in the testing of substitute payroll verification, a discrepancy was noted in the number of days tested. The auditor noted that "Gina to make up difference of 100 in June P/R." but there was no indication that this was actually done or followed up on by VTD.
- In testing disbursement transactions, one question in the audit program was whether the district used credit cards, and if so, the auditor should document the policies and procedures and consider selecting a sample of expenditures for testing. The auditor noted that the board approved a VISA card in FY 1997-98 for the superintendent; however, there was no indication that the policies and procedures were documented, and no indication of any testing.
- In testing disbursements, the auditor noted that the district did not put any jobs out for formal public bid, as required by law. The auditor was informed by the district that any new jobs were being handled by a construction management company, and would be advertised correctly. However, there was no indication of any follow up with the management company.
- In testing goods and services expenditures; several exceptions noted involved missing receiving information, purchase orders and receiving documents not agreeing, and one invoice being cancelled but paid. There was no follow up, nor was any internal control finding reported.

**FINDING 6—
Working paper
deficiencies**

The SCO reviewer noted several instances of noncompliance with the standards, as follows:

- Working papers did not always contain the nature and source of evidential matter. For example, the SCO reviewer was unable to identify whether some documents were prepared by the district or auditor.
- Working papers did not usually contain the objective, scope, and methodology. Most working papers did not clearly identify the purpose of the test, what was being tested, or how the test was performed.
- Working papers did not always contain sufficient information so that supplementary oral explanations were not required.
- Working papers did not usually contain evidence of supervisory review. There was no evidence of supervisory review on key audit areas, including the final review and approval checklist.

Additional working paper deficiencies noted include the following:

- Management Representation Letter: This letter (from the district) was not included in the working papers.
- Long-Term Debt: It appears that the auditor only updated the prior year schedule. No other documentation was provided.
- Building Fund accounts payable accruals: One item out of a population of three was selected for testing; however, it appears that no testing was actually performed because it was considered to be an immaterial amount (\$8,723.87 out of a total of \$14,233.56).
- Accounts Payable: According to the working papers, two adjusting entries should have been made; however, there was no explanation provided and no indication whether they were actually made.
- Student Body Funds: Based on the audit program, the auditor should have performed a subsequent receipts test; however, the auditor noted that this was not performed. No justification was provided.

In addition, financial statement documentation was deficient, as follows:

- The source of many amounts and information presented in the financial statements and notes to the financial statements was unclear. There was no support in the working papers for state revenue limit sources, receivables, and deferred revenue.
- Some amounts presented in the financial statements were supported solely by the unaudited J-200 report, such as accounts payable and due to other funds. However, there was usually no additional support documented in the working papers, and no indication of transaction

testing to support the amounts on the J-200 report or underlying documentation.

- The information in the notes to the financial statements was not consistently supported by the working papers, such as the market value of investments.

**FINDING 9—
State compliance testing
and reporting deficiencies**

There were written procedures for each state program; however, the VTD auditor did not consistently follow those procedures. Documentation in the working papers was not adequate to show the extent and results of work, nor did evidence support the opinions, comments, and findings reported.

The following deficiencies were noted:

- Staff Development Days: Three procedures were included in the K-12 Audit Guide; however, according to the audit program, the VTD auditor only tested to determine if staff development days appeared on the district calendar. No other documentation or testing was noted. The report on state compliance was not modified, as required.
- Kindergarten Enrollment: According to the audit program, VTD noted that it verified that all kindergarten students met the birthday requirement. However, there was no documentation to support this conclusion. Also, in the audit program for kindergarten enrollment, the auditor indicated that no pupils were retained; however, there was no documentation to support this.
- Reading Instruction Development Program: Four procedures were required by the K-12 Audit Guide; however, no testing was documented. The conclusion was based on discussions only. VTD indicated that some training was planned; however, there is no indication of any follow up. In addition, the report on state compliance was not modified, as required.
- Gann Limit Calculation: Two procedures were included in the K-12 Audit Guide; however, the SCO was unable to determine whether any testing was performed. The audit program contained references to a working paper that was not in the file.

**FINDING 10—
State compliance
sample selection
deficiencies and
expansion of testing**

Sampling methodology for state compliance testing was not adequate. The K-12 Audit Guide requires that representative samples be selected for testing. In addition, GAGAS Section 4.37 requires that working papers contain any sampling criteria used. However, the universe of transactions was not identified and sampling criteria was not consistently documented in the working papers. Therefore, SCO reviewers were unable to determine if samples were representative of the population. In addition, sample sizes appeared to be small, and testing was not expanded when exceptions were noted. For example, in testing attendance, eight students were selected for testing from month six; however, no population or universe was stated.

In addition, the following deficiencies were noted:

- State Instructional Materials: The working papers indicated that exceptions were noted in two of three items tested; however, testing was not expanded nor was a finding reported.
- Excused and Unexcused Absences: The working papers indicated that two of eight (25%) excused absences tested were missing a note. VTD noted that the discrepancies appeared to be isolated instances and did not appear to be a significant problem. Testing was not expanded nor was a finding reported.

Emery Unified School District, Fiscal Year 1998-99

FINDING 1— Due professional care deficiencies

Many items in the audit report were not supported in the working papers, such as stores inventory, revenues, and expenditures.

Many procedures were not clearly documented; therefore, the SCO was unable to reperform the audit steps. For example, for accounts payable, one item was selected for testing; however, no documentation supporting the testing was contained in the working papers.

Stores inventory was not tested and there was no documentation in the working papers supporting the reported amounts.

A judgment, estimated at \$28,000 to \$35,000, was rendered against the district; however, no contingent liability was established nor was it disclosed in the notes to the financial statements (refer to Finding 6).

Findings 9 and 10 also contain examples of due professional care deficiencies.

FINDING 2— Quality control deficiencies

Reviews of work done and judgments exercised do not appear to be consistently completed, which is in violation of VTD's stated policy.

Some audit programs were not approved by a VTD partner. The following are examples:

- Confirmations/bank account verification
- Disclosure checklist
- Report of regular day classes and enrollment
- Single audit master program
- Single audit and major program determination worksheet
- Test of transactions-Personnel and payroll
- Associated student body funds

Other working papers, such as review by independent auditor and auditor observation, had preprinted lines for the signature of the reviewer, but they were left blank. Some of these working papers pertained to audit exceptions and findings.

In addition, the many state compliance deficiencies indicate poor quality control (see Finding 9).

**FINDING 3—
Analytical review
deficiencies in planning**

Analytical reviews did not appear to be used in the planning stages. According to the working papers a review was performed; however, “analytical procedures” were not actually documented in the working papers.

**FINDING 4—
Deficiencies in
consideration of
computer processing
system in planning**

There was no documentation supporting VTD’s consideration of the effect of the district’s computer processing system on the audit.

**FINDING 5—
Internal control
deficiencies**

VTD did not clearly document its understanding of internal control. VTD used a questionnaire and performed limited walk-throughs to determine if controls were in place.

VTD used a questionnaire to document the district’s internal control structure; however, there was no indication of the source of the responses provided. In addition, some questions on the form were not answered; for example, whether there were policies and procedures for personnel access to data, assets, and computer programs, and if there were established procedures for authorizing transactions and approving changes to computer programs.

In the walk-through of disbursements, six transactions were selected for walk-through. Exceptions were noted in three of the six transactions; however, no comments were provided, no additional work was performed, and no internal control finding was reported. In addition, one of the six transactions selected was for a federal program. An exception was noted; however, there was no follow up or exception noted during federal program internal control or compliance testing.

**FINDING 6—
Working paper
deficiencies**

The SCO was unable to trace many of the amounts and information to the source. For example, the sources for all of the amounts on the cash lead sheet and the source for the amounts on the accounts receivable worksheet were not documented.

Some of the information presented in the audit report could not be traced to supporting working papers, including the notes to the financial statements. For example, the notes to the financial statements for fund balances and participation in public entity risk pools were not supported.

The testing methodology was not usually documented in the working papers. For example, for deferred revenue, 6 of 28 items were tested; however, the sampling methodology could not be determined.

The SCO auditors attempted to reperform many of the audit procedures that were documented; however, they were often unable to do so, and in some cases, the same results were not obtained. Some examples include state compliance testing for attendance, incentives for longer instructional day, and state instructional materials.

There was no supporting documentation for many areas of testing. For example, for accounts receivable testing, tick marks indicated that

various amounts “matches back up”; however, there was no identification as to what this consisted of.

Many working papers were not reviewed, or there was no documentation of review.

Some working papers contained lines for the reviewer’s initials, but they were left blank.

Several account balances were traced to the J-200; however, these are unaudited totals. For example, interfund transfers were traced to the J-200, but no other testing was documented in the working papers.

The accounts payable leadsheet contained an item referenced to a worksheet with no indication of the source of any of the numbers contained in it, there was no other supporting documentation. In addition, the deferred revenue documentation consisted of a worksheet that was referenced to the J-200 and J-390 reports, which are unaudited amounts. The worksheet indicated that selected items were verified through programs; however, there was no other supporting documentation.

In addition, the following deficiencies were noted:

- **Accounts Payable:** There was no documentation to support testing of accounts payable, except for an auditor-generated worksheet that was not supported.
- **Retiree Benefits:** The worksheet amounts were footed and cross-footed; however, there was no other documentation as to testing or explanations as to how payment amounts or life spans were determined or verified for validity or accuracy.
- **Contingencies:** A judgment, estimated at \$28,000 to \$35,000, was rendered against the district; however, no contingent liability was established, nor was it disclosed in the notes to the financial statements. Refer to Finding 1.
- **Revenues:** An analytical review of variances was performed; however, the procedures identified in the audit program were not consistently performed and the resolution of variances was not documented.
- **Accounts Receivable-Cafeteria:** Documents supporting the lead sheet amounts did not agree and the explanation regarding the discrepancy was not supported.
- **Revenues:** The individual state apportionment amounts per the J-200 did not agree to the financial statement amounts. Tax relief subvention amounts were included in the state apportionment amounts. As a result, local sources revenue per the J-200 did not agree with the amounts reported in the financial statements. However, the overall total of revenue limit sources per the J-200 agreed with the financial statement amounts, although there was no documentation explaining individual discrepancies.

**FINDING 7—
Deficiencies in
evaluating fraud, illegal
acts, and other
noncompliance**

VTD did not consider whether district management was dominated by a single individual or small group without compensating controls such as effective oversight by the governing body. VTD noted in the working papers that “Dr. Handy, Supt. and Gina Peters are key people at district, small staff limits segregation duties. District has management oversight.” However, Dr. Handy and Gina Peters were the “management oversight.” Based on the SCO’s review of the working papers, including answers to other questions and internal control narratives, district management was, in fact, dominated by a single individual or small group without compensating controls. In addition, the questionnaire noted that no audit committee existed and there was no internal audit function at the district. This indicated that management had oversight responsibility.

VTD’s evaluation and planning form included sections on conflict of interest and related party transactions. The following are some discrepancies noted during our review of the form:

- Question 17 asks, “Has the district adopted a specific policy on conflict of interest that specifies that personnel in a position of trust are not related to each other; employees are prohibited from having business dealings with companies affiliated with, or acting as major customers or suppliers of the District; transactions with officials of the District are adequately controlled and disclosed in the records; and such transactions occur only in the normal course of business and are legally authorized?” This question was answered “yes”; however, there was no documentation in the working papers indicating any follow up, or review of the conflict of interest policy.
- Question 18 refers to the district’s conflict of interest policy and any significant matters not covered by the conflict of interest policy. A notation next to the question indicates “No policy.” This was crossed out and changed to “None identified.” Both answers contradict the response to Question 17. There was no explanation provided in the working papers.
- Question 34D asks, “Are administrative, operating, or financial decisions dominated by a single person?” The question was answered “yes”; then changed to “no.” There was no explanation provided in the working papers.
- Question 34I asks, “Has a formal code of conduct, including policies on conflicts of interest, been adopted and are employees required periodically to make a declaration of compliance?” This was answered “no.” This answer conflicted with the answer to Questions 17 and 18.
- Questions 34L and 34M pertain to the policies and procedures over personnel access to data, assets, and computer programs, including transactions and changes to computer programs. These questions were not answered.

**FINDING 9—
State compliance testing
and reporting deficiencies**

VTD did not consistently apply the audit procedures in the state compliance areas for attendance, staff development days, kindergarten enrollment, independent study, Gann Limit calculation, class size reduction program, Morgan Hart class size reduction program, and state instructional materials fund as follows:

- **Attendance:** The working papers indicated that the internal control survey for attendance was in the system file. However, VTD did not provide SCO reviewers with an internal control survey for FY 1998-99. In addition, none of the prior internal control surveys in the system file had been updated, nor was there any indication of review for FY 1998-99. The working papers indicated that one document was tested for accuracy by cross-footing; however, the SCO reviewers identified an error on the document that had not been detected by the firm.
- **Staff Development Days:** Limited testing appears to have been performed. The audit report indicated that all three required procedures were performed; however, VTD did not examine contemporaneous documents to determine the validity of the claim for reimbursement of instructional time and staff development reform program days. In addition, staff development days identified by VTD did not agree to district records. There was no explanation in the working papers and state compliance report for why the suggested audit procedures were not performed, and no finding was reported.
- **Kindergarten Enrollment:** None of the four suggested audit procedures were performed. The site selected for kindergarten enrollment testing was a high school; therefore, no testing was performed, as there were no kindergarten classes at the high school. However, the audit report indicated that all four audit procedures were performed.
- **Independent Study:** The audit report indicated that 13 procedures related to independent study were performed; however, no ADA was claimed on the J-18/19 report and no audit procedures were performed.
- **Gann Limit Calculation:** Numbers on the form were tied to the J-200 report, which includes unaudited totals. No other testing was documented. The K-12 Audit Guide requires the auditor to verify that the data used by the district is accurate, ensuring that prior year ADA matches the prior year calculation. The report on state compliance indicated that all suggested procedures were performed.
- **Class Size Reduction Program:** The testing period did not cover the required period. VTD tested the period of September 9 to December 16; however, the required period should have been September 10 to April 15. As a result, testing included a day prior to the start of the school year, and excluded the period from December 17 to April 15. Therefore, the average class sizes required to be calculated may have been inaccurate. In addition, the working papers noted that an amount was not included in the class size

reduction calculation and that the district would be making a revision; however, there was no indication that this was actually done. No finding was included in the audit report.

- Morgan Hart Class Size Reduction Program: The reported numbers were tied to the J-200, which are unaudited totals. In addition, based on the working paper documentation, SCO reviewers recalculated the total that should have been claimed. The claim was overstated by \$2,422 (12%). No finding was included in the audit report.
- State Instructional Materials Fund: VTD noted that 25% of the sample tested was not supported by documentation, which was equal to 17% (\$2,238) of the total dollar amount tested (\$12,845). However, the sample was not expanded. No finding was included in the audit report.

**FINDING 10—
State compliance
sample selection
deficiencies and
expansion of testing**

Sampling methodology for state compliance testing was not adequate. The K-12 Audit Guide requires that representative samples be selected for testing. In addition, GAGAS Section 4.37 requires that working papers contain any sampling criteria used. The universe of transactions was not identified and sampling criteria was not consistently documented in the working papers. Therefore, SCO reviewers were unable to determine if samples were representative. In addition, sample sizes appeared to be small, and testing was not expanded when exceptions were noted.

For example, for state instructional materials, four transactions were selected for testing. The universe of transactions was not identified, and the sampling methodology was not documented. In addition, one exception was noted; however, testing was not expanded, nor was a finding reported.

In addition, for staff development days, VTD's audit program requires the auditor to review a sample of school site or school development plans, and determine that each staff development day ties to the approved staff development program. There was no documentation indicating the size or characteristics of the sample. The audit program only contains the notation, "Reviewed-OK."

**FINDING 11—
Federal program internal
control deficiencies**

The single audit questionnaire was not completed. The questionnaire addresses the internal control (control environment, risk assessment, control activities, information and communication, and monitoring) components for each of the single audit OMB Circular A-133 compliance areas and is the basis for the risk assessment. Questions answered "Yes" that required an explanation on the questionnaire were not explained. The firm did not document why assurance is placed on controls. There was no documentation of the testing plan for internal control assertions as required by the OMB Circular A-133 Compliance Supplement, Part 6, for each major program. The basis for the conclusion for federal internal control was not documented. Two findings from the prior audit related to federal compliance, but these were not considered in the VTD's current year control risk assessment.

**FINDING 12—
Federal program
compliance deficiencies**

In the working papers for federal compliance, the components required to be tested by OMB Circular A-133 were marked as “N/A” by the firm; however, no explanations were provided.

The firm’s audit program noted that several federal compliance requirements applicable to the Child Nutrition Cluster (School Breakfast Program (10.553) and National School Lunch Program (10.555)) according to the OMB Circular A-133 Compliance Supplement were “N/A” (not applicable); however, there was no explanation for why these compliance requirements did not apply. The components noted as “N/A” included the following:

- Cash management
- Equipment and real property management
- Program income
- Reporting
- Subrecipient monitoring

There was no audit program for the 21st Century program. The working papers only contained a description of the program. No testing was performed; however, the 21st Century program was identified as a major program in the Schedule of Expenditures of Federal Awards. Tests are required for each program classified as major.

Emery Unified School District, Fiscal Year 1999-2000

**FINDING 1—
Due professional care
deficiencies**

Several items in the audit report were not supported in the working papers:

- Postemployment benefits activity and ending balance; and
- Note 11, Participation in Public Entity Risk Pools and Joint Powers Authorities.

Use of good auditor judgment in choosing tests and procedures was questionable. For example, student body fund amounts were not traced to supporting documentation. In addition, the reduction in long-term debt was not traced to a cancelled check or other substantive verification that the payment was actually made.

Deficiencies were also noted in state compliance testing (refer to Findings 9 and 10).

Steps or procedures were left out in the documentation process; therefore, the SCO reviewers could not reperform the audit steps or procedures. For example, no cash reconciliations were documented; therefore, the SCO reviewers were unable to verify the cash balances.

Inventory balances per the district’s records were the same as for FY 1998-99. This may have been an indication that the district did not properly account for FY 1999-2000 activity; however, this was not noted or evaluated by VTD.

In addition, general fund materiality was determined to be \$10,700 based on VTD's working papers. General fund stores inventory, according to the district's records, was \$10,948, which was considered to be material, based on VTD's determination; however, no testing was performed. An auditor's note in the working papers stated, "Client has not performed any inventory procedures . . . since prior year. The records are considered unauditable." However, the reason why the records were considered to be unauditable was not documented, and no finding or scope limitation was reported.

The audit working papers indicated that there was "no payroll clearing" account. However, this was inconsistent with an audit finding included in the report, which was that the district had not performed any bank reconciliations for the payroll clearing account (see Finding 6).

**FINDING 2—
Quality control
deficiencies**

Reviews of work performed were not consistently documented. In addition, judgments exercised by audit staff did not appear to have been adequately evaluated during the review process. For example, stores inventory was not tested to determine if the reported amounts were valid, as the balance was the same as the prior year. In addition, the many state compliance deficiencies indicate poor quality control (see Finding 9).

**FINDING 3—
Analytical review
deficiencies in planning**

Documentation to support analytical review procedures performed in planning the nature, timing, and extent of other auditing procedures was deficient. The working papers included percentage change comparisons between the prior and current fiscal years for dollar and ADA amounts, and comparisons to budget; however, there was no documentation of any analysis or evaluation of the variances.

**FINDING 4—
Deficiencies in
consideration of computer
processing system in
planning**

The effect of the district's computer processing system on the audit was not clearly documented in the working papers. Documentation reviewed in VTD's system file discusses the attendance process for each school site and the adult school; however, the overall effect was not documented, nor were other computer processing systems considered.

**FINDING 5—
Internal control
deficiencies**

Control risk was assessed at maximum. The firm did not document the control risk for assertions embodied in account balance, transaction class, and disclosure components of the financial statements as required by SAS 78. Although control risk was used in planning the audit, it was assessed on an overall basis only.

Deficiencies were noted on several of the internal control questionnaires. Some example are as follows:

- Organization and Personnel Practices: Several questions were answered "no"; however, there was no auditor comment, explanation, or discussion. Also, some questions were not answered.
- Internal Control Survey, Payroll: Several questions were answered "no"; however, there was no auditor comment or explanation.

**FINDING 6—
Working paper
deficiencies**

There was no evidence of supervisory review on many working papers. Some examples are as follows:

- Internal control survey—Revolving cash
- Internal control survey—Site cash collections
- Internal control survey—Property plant and equipment

The amounts reported for postemployment benefits did not agree to the working papers. The current year activity and ending balance per the financial statements were \$68,447 and \$198,144, respectively; however, the amounts per the working papers were \$12,232 and \$117,465. There was no explanation in the working papers regarding the discrepancies and no reference to an adjusting journal entry or reclassification.

The revenues and expenditures audit program section for wrap up and conclusion was not completed.

The revenues and expenditures audit program indicates that there is “no payroll clearing” account. However, this is in disagreement with an audit finding included in the report for not having performed any bank reconciliations for the payroll clearing account (see Finding 1).

**FINDING 9—
State compliance testing
and reporting deficiencies**

Several deficiencies in performing state compliance procedures were noted, as follows:

- Incentives for Longer Instructional Day: Based on the SCO review of the working papers, kindergarten instructional minutes offered equaled 200 minutes for both the morning and afternoon sessions. However, according to the audit report, there were 210 minutes for each session. Consequently, the schedule of instructional time included in the audit report was incorrect.
- Class Size Reduction Program (Option One Classes): The district’s J-7CSR worksheet indicated that two teachers were new CSR teachers; however, the auditor’s attribute testing worksheet indicated that these same two teachers were not new CSR teachers.
- Schiff-Bustamante Standards-Based Instructional Materials: Procedure 4, which requires the auditor to review and test compliance for grades 9-12, was not completed; however, the report on state compliance indicates that all four required procedures were performed.

**FINDING 10—
State compliance
sample selection
deficiencies and
expansion of testing**

Sampling methodology for state compliance testing was not adequate. The K-12 Audit Guide requires that representative samples be selected for testing. In addition, GAGAS Section 4.37 requires that working papers contain any sampling criteria used. The universe of transactions was not identified and sampling criteria was not consistently documented in the working papers. Therefore, SCO reviewers were unable to determine if samples were representative. In addition, sample sizes appeared to be small, and testing was not expanded when exceptions were noted. For example, for adult education, ten students were selected for testing, but the total population or sampling methodology was not documented.

In addition, for excused absences, five students were selected for testing; however, the population was not identified. However, one exception was noted. The VTD auditor noted that it “appears to be an isolated incident.” Testing was not expanded, nor was a finding reported.

**FINDING 11—
Federal program internal
control deficiencies**

The single audit control risk was assessed at low. This assessment was based on a questionnaire that addressed the internal control components for each of the single audit OMB Circular A-133 compliance areas.

There were two findings from the prior year’s audit related to federal compliance; however, one of these findings still existed. In addition, fraud allegations had been made against the former superintendent. This would not support a low-risk assessment.

**FINDING 12—
Federal program
compliance deficiencies**

In the working papers for federal compliance, the components required to be tested by OMB Circular A-133 were marked as “N/A” by the firm; however, no explanations were provided.

The firm’s audit program noted that several federal compliance requirements applicable to the Child Nutrition Cluster (School Breakfast Program (10.553) and National School Lunch Program (10.555)) according to the OMB Circular A-133 Compliance Supplement were “N/A” (not applicable); however, there was no explanation for why these compliance requirements did not apply. The components noted as “N/A” included the following:

- Cash management
- Equipment and real property management
- Program income
- Reporting
- Subrecipient monitoring

Fremont Unified School District, Fiscal Year 1999-2000

**FINDING 1—
Due professional care
deficiencies**

Use of good auditor judgment in selecting tests and procedures to be performed is questionable. For example, the firm did not observe inventory; however, some test counts were performed. The firm’s audit program required price testing on a minimum of ten items; however, it appears that only six items were actually tested. There was no written justification provided for the reduction in testing.

Several items in the financial statements were not supported in the working papers. For example, total cash and investments and accounts payable presented in the audit report did not agree to supporting documentation.

Steps or procedures were not documented in the working papers; therefore, the SCO reviewers were unable to reperform certain audit procedures.

The issues noted in Findings 9 and 10 also show lack of due professional care in testing for state compliance.

**FINDING 2—
Quality control
deficiencies**

Reviews of work performed were not consistently documented. The following are some examples of internal control surveys that had no evidence of supervisory review:

- Revolving fund cash
- Purchasing/receiving
- Payroll
- Federal single audit
- Associated student body

Supervisory reviews were missing in key audit areas such as the revenues and expenditures audit program and the disclosure checklist.

In addition, the many state compliance deficiencies indicate poor quality control (see Finding 9).

**FINDING 5—
Internal control
deficiencies**

Testing or audit programs did not appear to be modified as a result of the internal control assessments. The internal control working papers did not indicate whether a final control risk assessment was made.

Conclusions were not documented regarding the evaluation of control risk and the evaluation of risk that material misstatements existed in the financial statements.

**FINDING 6—
Working paper
deficiencies**

The audit report was not fully supported by the working papers. Amounts in the financial statements and several notes to the financial statements (for example, accounts payable) did not agree to the working papers. The total liabilities per the working papers was \$10,322,184 as compared to \$11,610,067 per the audit report. The \$1,287,883 variance was not addressed in the working papers.

For cash and investments, the amount presented in the financial statements was \$1,075,855 more than the amount documented in the working papers. No explanation for the discrepancy was noted.

For long-term debt, the amount to be provided for retirement of long-term debt presented in the financial statements was \$94,270 less than the amount documented in the working papers. Per the working papers, the difference was due to a larger deduction to the capital lease balance than the amount reflected on the lead sheet. However, the change in the capital lease deduction amount from \$464,024 to \$558,294 was not noted in the general long-term debt working papers.

Supervisory reviews were missing in key audit areas. For example, there was no evidence of supervisory review of the internal control working papers for revolving cash, accounts payable, purchasing, or student body funds.

The conclusions on working papers were not specifically stated. The conclusions were usually referenced back to the audit objectives.

No initials or dates of the preparer and reviewer were noted on several state compliance working papers.

FINDING 9—**State compliance testing
and reporting deficiencies**

Several deficiencies in state compliance testing were noted, as follows:

- **Staff Development:** This program was not properly tested as the firm did not correctly apply the suggested audit procedures. The firm selected eight schools to test; however, when non-compliance was noted, it was not recognized as an audit finding and not reported. For example, the working papers showed that two of the staff development days for Chadbourne Elementary were “undecided” in terms of the topic. The related funding for these two days should have been disallowed because of the undecided nature of the staff development days. Hirsch Elementary was also selected for testing. The purposes for the three staff development days were Back to School Night, Winter Party, and Valentine’s Party. All three staff development days and the related funding should have been disallowed. In addition, for Hirsch Elementary, there is a notation that “Per ICQ and inquiry, all SDD are on minimum days and are taking place after the students left school. No further testing will be needed.”

The working papers also showed that the staff development days for Glenmoor Elementary, Weibel Elementary, and Walters Jr. High were selected for testing. The testing working papers contained the comment “See system file for SDD of the whole district.” The system file did not contain any discussion of staff development days for these school sites. The report on state compliance indicates that all required procedures were performed.

- **Kindergarten Enrollment:** For Glenmoor Elementary, the working papers contained a retention form that was clearly not compliant as it did not contain the required elements. The firm did not recognize that the form was non-compliant; consequently, no audit finding was reported.
- **Incentive for Longer Instructional Day—School Districts:** There was no supporting documentation for the number of minimum days in the school year or the number of school days other than the regular day. In addition, copies of school bell schedules were included in the working papers; however, there was no indication if they were approved at the district office and whether they were the final accepted schedules.
- **State Instructional Materials Fund:** Suggested audit procedure 7 in the K-12 Audit Guide requires a ten-day notice of the hearing. The working papers indicated that the district did not comply with this requirement, as there was only a two-day notice. However, no finding was noted or included in the audit report. The firm should have questioned all state funding received for state instructional materials due to non-compliance.
- **Digital High School (DHS):** Suggested audit procedure 5 in the K-12 Audit Guide requires a determination of whether the funds were spent in accordance with the approved DHS program grant application. However, there was no support in the working papers for this procedure. The report on state compliance indicates that all five required procedures were performed.

**FINDING 10—
State compliance sample
selection deficiencies and
expansion of testing**

The sampling methodology for state compliance testing was not adequate. The K-12 Audit Guide requires that representative samples be selected for testing. In addition, GAGAS Section 4.37 requires that working papers contain any sampling criteria used. The universe of transactions was not identified and sampling criteria was not consistently documented in the working papers. Therefore, SCO reviewers were unable to determine if samples were representative. In addition, sample sizes appeared to be small, and testing was not expanded when exceptions were noted. For example, for the Incentive for Longer Instructional Day–School Districts, 7 out of 41 schools were selected for testing; however, it was not documented how the type of school or number of schools was determined, or the sampling methodology used.

**FINDING 11—
Federal program internal
control deficiencies**

There was no final assessment of control risk for major programs.

Internal controls for the major programs, Child Nutrition Cluster and Special Education, were tested; however, it was not clear whether testing was modified as a result of a control risk assessment for major programs.

**FINDING 12—
Federal program
compliance deficiencies**

In the working papers for federal compliance, the components required to be tested by OMB Circular A-133 were marked as “N/A” by the firm; however, no explanations were provided.

The firm’s audit program noted that several federal compliance requirements applicable to the Child Nutrition Cluster (School Breakfast Program (10.553) and National School Lunch Program (10.555)) according to the OMB Circular A-133 Compliance Supplement were “N/A” (not applicable); however, there was no explanation for why these compliance requirements did not apply. The components noted as “N/A” included the following:

- Cash management
- Equipment and real property management
- Program income
- Reporting
- Subrecipient monitoring

Federal compliance testing appeared to be limited and did not adequately fulfill the OMB Circular A-133 compliance requirements, and documentation was inadequate to support the work performed and the results.

Newark Unified School District, Fiscal Year 1999-2000

**FINDING 1—
Due professional care
deficiencies**

Auditor judgment in selecting tests and procedures to be performed was not consistently documented (see Finding 6 for examples).

Inventory was tested; however, the testing was deficient; as follows:

- Inventory quantities were randomly sampled based on a sample selection of 27 items. Testing was expanded by two additional items when exceptions were noted in the original sample. Of the total 29

items sampled, 4 exceptions were noted, which was a 14% error rate. However, there was no follow up and no finding was reported.

- Less than 1% of stores inventory was selected for testing, and exceptions were noted for all items tested. However, the sample was not expanded, yet the error rate was projected to the total population and determined to be immaterial.

The extent and method of substantive testing is not related to the assessed risk levels, and sample size expansion did not usually occur, even when a substantial exception rate occurred, as noted in inventory testing.

Information in the audit report was not adequately supported in the working papers. For instance, the notes to the financial statements for accounts receivable and accounts payable were not supported in the working papers.

Steps and procedures were not sufficiently detailed in the working papers to allow the reviewer to reperform the audit steps and procedures. For instance, for expenditure testing, transactions were to be “agreed to backup,” however, there was no description or explanation of the type of backup tested (i.e., invoices, shipping documents, purchase orders).

Deficiencies were also noted in state compliance testing (see Findings 9 and 10).

FINDING 2— Quality control deficiencies

Reviews of work performed were not consistently documented. In addition, judgments exercised by audit staff did not appear to have been adequately evaluated during the review process.

Supervisory reviews were lacking in key audit areas. Some examples of audit programs or major areas where there was no evidence of supervisory review include the following:

- Adjusting journal entries and reclassification journal entries
- Audit program for categorical programs
- Audit program for Child Nutrition cluster
- Audit program for budget monitoring
- Audit program for student body funds
- General procedures section

In addition, several other working papers had preprinted lines provided for supervisory review, but they had not been signed.

In addition, the many state compliance deficiencies indicate poor quality control (see Finding 9).

**FINDING 3—
Analytical review
deficiencies in planning**

There was no evidence that analytical review procedures were performed during the planning stages of the audit. Analytical procedures were performed; however, they were performed and analyzed during the final stages of the audit. The working papers contained no documentation of how the auditor determined the nature, timing, and extent of audit procedures.

**FINDING 5—
Internal control
deficiencies**

Control risk was assessed at maximum. The firm did not document the assessed control risk for the assertions embodied in the account balance, transaction class, and disclosure components of the financial statements as required by SAS 78.

Questionnaires were used to document the district's internal control structure. However, the questionnaires did not indicate who provided the answers or whether the questions were discussed with the district.

On the evaluation and planning form, there was no response to the question, "Are financial and statistical reports prepared for management on a timely basis and frequently enough to be useful?"

There was no stated conclusion that internal control policies and procedures were in place and whether or not they were properly operating.

**FINDING 6—
Working paper
deficiencies**

The conclusions on working papers were not consistently stated. The conclusions were usually referenced back to the audit objectives. For example, all audit programs contained a preprinted conclusion which stated, "applied procedures sufficient to achieve the audit objectives."

Audit steps and procedures were not always documented. Therefore, the SCO reviewer was unable to reperform work. For example, for deferred revenue, the working papers noted that items were verified through programs. However, there were no detailed steps or procedures identified.

The audit report was not fully supported by the working papers. For example, revenue and expenditure balances in the working papers did not agree to the financial statements.

Deficiencies were noted in the testing for the following:

- Cash: Confirmation amount did not reconcile to the financial statements.
- Deferred Revenue: The supporting documentation was an auditor-prepared worksheet that was tied to the client-generated J-200 and J-390. Specific items were noted as being verified through programs; however, no other supporting documentation was provided.
- Fund Balance—Reserved: No testing was documented except for verifying the beginning J-200 balance to the prior-year audit report. VTD should have determined that the fund reservations were accurate and appropriate.

- **Unreserved–Designated:** No testing was documented except for verifying the beginning J-200 balance to the prior-year audit report. VTD should have determined that the Unreserved-Designated amounts were accurate and appropriate.
- **Revenues:** The working papers did not support the amounts presented in the financial report. State apportionments presented in the J-200 did not agree to the financial statements. Tax relief subvention amounts were included in the State apportionment amount; therefore, local sources revenue did not agree to the J-200 or financial statements. There was no indication that these amounts were verified or traced to the general ledger or other supporting documentation.
- **Expenditures:** The working papers did not support the amounts presented in the financial report. The amounts presented in the J-200 did not agree to the financial statements. There was no indication that expenditures were verified or traced to the general ledger or other supporting documentation.

The notes to the financial statements were not supported and could not be readily traced to the working papers for the following:

- **Cash:** The numbers on the cash spreadsheet in the working papers could not be readily traced to the note.
- **Accounts Receivable:** There was no documentation supporting the note.
- **Accounts Payable:** There was no documentation supporting the note.
- **Fund Balances:** There was no documentation supporting the note.
- **General Long-Term Debt:** There was no documentation supporting the note.
- **Participation in Public Entity Risk Pools and Joint Powers Authorities:** There was no documentation supporting the note.

Other working paper deficiencies were noted, as follows:

- **Expenditures–Budget versus Actual:** The general fund amounts did not agree to the working papers, although the other fund amounts did.
- **The Special Education, National School Lunch, Title I, and Summer Youth Employment programs** were not verified to the grant award or other supporting documents.
- **Compensated Absences:** Five rates were traced to payroll records; however, there was no documentation that the accrued hours were verified.
- **Representation Letters:** Only one out of three legal representation letters were documented. It appears that verbal confirmations were made. There was no documentation as to when the call was made or who confirmed there were no liabilities. The one letter included in the

working papers indicated the district could be liable for \$25,000 in attorney's fees but there was no disclosure in the financial report. There was no explanation as to why no disclosure was necessary.

- Budgeted to Actual: An analysis of budgeted to actual amounts was not documented.

**FINDING 7—
Deficiencies in
evaluating fraud,
illegal acts, and other
noncompliance**

The fraudulent risk assessment form indicated that Y2K issues could have a significant financial impact on the district; however, no follow up was noted in the working papers. The form indicated that the fixed asset detail was not current; however, no follow up was noted.

The evaluation and planning form indicated that both the director of accounting and fiscal services had new duties during the fiscal year being audited; however, there was no follow up noted. In addition, there was no discussion of this in the management representation letter.

The evaluation and planning form noted that no modifications were necessary to the audit program; however, there was no justification provided.

**FINDING 9—
State compliance testing
and reporting deficiencies**

Several deficiencies in performing state compliance procedures were noted, as follows:

- Staff Development: There was no evidence that all of the procedures required by the K-12 Audit Guide were performed. This includes verifying that the staff development day is at least as long as a normal instructional workday and determining that staff development days included specific attributes. The report on state compliance indicates that all three procedures were performed.
- Incentives for Longer Instructional Day: The SCO reperformance of the audit procedures resulted in different amounts than those documented in the working papers. VTD had calculated 25 minimum days; however, the SCO reviewers calculated minimum days to be 31. Therefore, the information presented in the schedule of instructional time was incorrect.
- Class Size Reduction (Option One): There was no evidence that the auditor determined the average daily class size for specified sample classes. However, the report on state compliance reflected that all 12 procedures were performed.
- Morgan Hart (Grade 9) Class Size Reduction: The working papers indicated that there was a finding regarding the district not having documents to support the claim for Morgan Hart funds. It appears that the district overclaimed 3 full-year equivalent enrollment (FYEE). However, this was not reported as an audit finding and there was no indication of the disposition of the finding.
- State Instructional Materials Fund: There was no evidence that the auditor determined whether the district board made a determination, through a resolution, as to whether each pupil in each school in the district has, or will have before the end of that fiscal year, enough

textbooks and other instructional materials in each subject consistent with the content and cycles of the curriculum framework adopted by the state board. The audit program indicates that this procedure was performed; however, there was no supporting documentation. The report on state compliance stated that all eight steps were performed.

**FINDING 10—
State compliance
sample selection
deficiencies and
expansion of testing**

Sampling methodology for state compliance testing was not adequate. The K-12 Audit Guide requires that representative samples be selected for testing. In addition, GAGAS Section 4.37 requires that working papers contain any sampling criteria used. The universe of transactions was not identified and sampling criteria was not consistently documented in the working paper. Therefore, SCO reviewers were unable to determine if samples were representative. In addition, sample sizes appeared to be small, and testing was not expanded when exceptions were noted.

Deficiencies were noted in the state compliance sample selection, as follows:

- Kindergarten Enrollment: Three pupils out of a population of approximately 505 kindergartners were selected for testing, which was approximately .006% of the population. The K-12 Audit Guide requires the auditor to select a representative sample for testing.
- Attendance Accounting: Two elementary school sites were selected for testing; however, the working papers indicated that only one school site was actually tested. There was no explanation or justification as to why only one school site was tested.

**FINDING 11—
Federal program internal
control deficiencies**

The review of federal program internal control was based on internal control questionnaires in the general evaluation and planning questionnaire. Specific support for federal internal controls was not evident in the working papers.

The planning federal programs questionnaire was designed to cover multiple years. There was no specific reference to the year being audited.

**FINDING 12—
Federal program
compliance deficiencies**

In the working papers for federal compliance, the components required to be tested by OMB Circular A-133 were marked as “N/A” by the firm; however, no explanations were provided.

The firm’s audit program noted that several federal compliance requirements applicable to the Child Nutrition Cluster (School Breakfast Program (10.553) and National School Lunch Program (10.555)) according to the OMB Circular A-133 Compliance Supplement were “N/A” (not applicable); however, there was no explanation for why these compliance requirements did not apply. The components noted as “N/A” included the following:

- Cash management
- Equipment and real property management
- Program income
- Reporting
- Subrecipient monitoring
- Procurement and suspension and debarment

There was a federal program finding regarding multi-funded position reporting deficiencies, presented in the audit report; however, the working papers did not contain any reference to this finding. No exceptions for federal programs were noted in the working papers.

In addition, the audit program for the special tests and provisions requirement was not completed.

Mission Valley Regional Occupational Program, Fiscal Year 1999-2000

FINDING 9— State compliance testing and reporting deficiencies

The audit report on state compliance stated that all four audit procedures related to attendance reporting were performed. However, the SCO's review disclosed that the following procedures were not performed:

- Audit procedure 3a requires the auditor to reconcile the monthly totals on the site's attendance summary to the summary maintained by the LEA for the annual attendance reports. However, there was insufficient evidence in the working papers to support that this step was performed.
- Audit procedure 3c requires the auditor to select a representative sample of classes (teachers) and trace the monthly totals from the monthly report to the attendance registers, scantron summaries, etc. However, there was no evidence in the working papers to support that this step was performed.
- Audit procedure 4 requires the auditor to select a sample of excused absence documentation (notes, logs, etc.) and compare to documentation supporting ADA reported to the State to verify that excused absences were not claimed for apportionment. However, there was no evidence in the working papers to support that this procedure was performed.

There were no explanations in the working papers or in the report on state compliance regarding why the procedures were not performed, or if alternative procedures were applied.

**Attachment 1—
Firm's Response to Draft Report**

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Vavrinek, Trine, Day & Co., LLP
Certified Public Accountants & Consultants

VALUE THE DIFFERENCE

June 14, 2004

Cassandra Moore-Hudnall, Chief
Financial Audits Bureau
State Controller's Office – Division of Audits
P. O. Box 94250
Sacramento, California 94250-5874

Dear Ms. Moore-Hudnall:

Enclosed please find our response to your draft report dated April 2004 related to your quality control review of Vavrinek, Trine, Day & Co., LLP (Pleasanton Office) and your review of the audit working papers for the Firm's audits of the Emery Unified School District for the years ended June 30, 1998, 1999, and 2000; the Fremont Unified School District (FUSD) for the fiscal year ended June 30, 2000; the Newark Unified School District (NUSD) for the fiscal year ended June 30, 2000; and the Mission Valley Regional Occupational Program (MVROP) for the fiscal year ended June 30, 2000.

We request that you contact us should further revisions to the draft report be made prior to its issuance in final form. We request the opportunity to revise our response accordingly for any revisions made by SCO. In addition, we request the SCO include our response in its entirety along with the distribution of the SCO report. Should the SCO post its report on their website or in anyway distribute its report electronically, we request our response accompany such posting and distribution.

Should you have any questions, or require additional information, please feel free to contact me.

Sincerely,

A handwritten signature in cursive script that reads 'Linda S. Todd'.

Linda S. Todd
of Vavrinek, Trine, Day & Co., LLP

LST:lst



Vavrinek, Trine, Day & Co., LLP
Certified Public Accountants & Consultants

VALUE THE DIFFERENCE

June 14, 2004

Cassandra Moore-Hudnall, Chief
Financial Audits Bureau
State Controller's Office – Division of Audits
P. O. Box 94250
Sacramento, California 94250-5874

Dear Ms. Moore-Hudnall:

We are in receipt of your revised draft report dated April 2004 related to your quality control review of Vavrinek, Trine, Day & Co., LLP (Pleasanton Office) and your review of the audit working papers for the Firm's audits of the Emery Unified School District for the years ended June 30, 1998, 1999, and 2000; the Fremont Unified School District (FUSD) for the fiscal year ended June 30, 2000; the Newark Unified School District (NUSD) for the fiscal year ended June 30, 2000; and the Mission Valley Regional Occupational Program (MVROP) for the fiscal year ended June 30, 2000.

We disagree with the SCO conclusion and opinion regarding this quality control review. In addition, we disagree with many of the examples cited in the SCO report that were cited as support for the conclusion and opinion. Many of the statements made regarding the examples cited do not represent an accurate portrayal of the working papers.

VTD's Response to Finding 1 – Due Professional Care

We disagree with the SCO that due professional care was not exercised in the conduct of the audits and the preparation of the related reports. We disagree with many of the other findings contained within the report and those contained in the summary of findings by district and year. The SCO references Findings 2 through 12 as additional support for the conclusion. As enumerated below, we disagree with many of these findings.

The SCO provides as examples to support their finding regarding Due Professional Care, the lack of testing of inventory, issues regarding the payroll clearing account, noncompliant retention form, and deficient attendance testing. We dispute or agree with these examples as follows:

Inventory

SCO has made an assumption about the materiality levels calculated by VTD that is not correct and has cited standards that are not applicable under the circumstances.

Materiality is a matter of professional judgment and involves both quantitative and qualitative considerations (AU 312.10). Our quantitative considerations about materiality are based upon guidance contained in the Practitioners Publishing Company's *Audits of Local Governments (PPC)*, which is a recognized industry standard used by many accounting firms throughout the United States. This publication has been subjected to a review of its quality and control in the development of the guide in accordance with the standards of the SEC Practice Section of the AICPA. Based upon this guidance, VTD calculates preliminary quantitative materiality levels using the

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larger of total assets or total revenue of each fund as a base. Additional amounts and percentages (amounts and percentages applied are determined on the level of the total assets or total revenues) are applied to the base to calculate Planning Materiality. Another percentage is applied to Planning Materiality to arrive at Tolerable Misstatement. A point between not less than 1/6 and not more than 1/3 of Tolerable Misstatement is then established as a Determined Amount. Planning Materiality represents that amount that is applied by the Auditor as the acceptable limit of misstatement of financial statements and applies to the fund financial statements taken as a whole. Tolerable Misstatement is applied at the account balance level. The Determined Amount is used in determining individual items of an account balance or transaction class subjected to detailed tests.

This concept was explained and discussed with representatives of SCO at the exit conference conducted on June 18, 2002 and again on October 6, 2003. This second explanation occurred after providing SCO with further explanation and appropriate standards related to materiality and scope limitations in writing. At the exit conference in October, the SCO representative had indicated they would not include the inventory issue in their next draft.

The SCO cites EUSD FY 1998-99 work papers as an example where there was no testing of the inventory account balance. In our Audit Planning Memo located in the General Information section of the audit work papers A4 Item 10, we have documented at Inventory "No testing to be performed – Gen/Café stores are not material". At work paper A5.1, Planning Materiality was calculated at \$49,966 and \$7,874 for the General Fund and the Cafeteria Fund, respectively. Tolerable misstatement was calculated at \$37,475 and \$5,905 for the General Fund and the Cafeteria Fund, respectively. Stores inventory recorded on the financial statements at June 30, 1999 were \$10,948 for the General Fund and \$818 for the Cafeteria Fund. Clearly, these amounts are not material.

The SCO cites EUSD FY 1999-2000 work papers as an example where inventory procedures were not performed. At work paper A5 page 4 Planning Materiality was calculated at \$56,844 and \$8,563 for the General Fund and the Cafeteria Fund, respectively. Tolerable misstatement was calculated at \$42,633 and \$6,422 for the General Fund and Cafeteria Fund, respectively. Stores inventory recorded on the financial statements at June 30, 2000 were \$10,948 for the General Fund and \$819 for the Cafeteria Fund. Clearly, these amounts are not material. The auditors determined that the inventory had not been updated since the prior year and was unauditable. The inventories would not have been material based on our knowledge of the District and performing alternative procedures would not have been justified.

In both examples cited, VTD determined that these balances were not material and therefore, not subject to audit tests. As such, it was determined that a scope limitation was not warranted under the circumstances since the nature and magnitude of the potential effects of not performing inventory observation procedures was not significant to the financial statements. Performing work on immaterial transactions or balances is not necessary to obtain sufficient and competent evidential matter to support our opinion and is not efficient. Audit work that is necessary to form our opinion is required regardless of the difficulty or cost involved. However, professional standards contemplate that audits are to be done efficiently for reasonable costs. Performing audit procedures on an \$800 inventory would clearly not be necessary to form an opinion on the fairness of presentation of the financial statement taken as a whole.

We have provided citations for appropriate standards regarding materiality and scope limitations in the Appendix attached to this response.

Payroll Clearing Account

The District instituted a Payroll Clearing Account for the first time during the year of audit. The addition of the account was not noted during interim work but was noted at year-end. Additional information is noted throughout the audit and the lack of a notation on the interim work paper that the Payroll Clearing Account existed would not

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have prohibited the work papers from being understood. Clearly the account existed and comments were made regarding reconciliation of the account during the year-end work. We disagree that this is an example of a lack of due professional care.

Noncompliant Kindergarten Retention Form

We agree with SCO that one of the Kindergarten retention forms was not the State approved form.

Deficient Attendance Testing

We disagree with the SCO regarding the attendance accounting testing being deficient. Each year our summary planning document is prepared and at that time it is determined which schools will be selected for testing. This is often done in conjunction with Management. We appropriately determined which schools would be tested and documented as such in our planning document. The SCO is referring to a long-term planning document included in a permanent file that was prepared in prior years that was not intended to be used for the planning of the fiscal year under audit. We agree, that this caused the representatives to become confused, however, we disagree that this example represents a lack of due professional care.

Finding 2 – Quality Control Deficiencies

We disagree with the SCO that all audit files contained deficiencies in documenting these reviews. Our reviews are documented on our Audit Supervision and Review checklist. In addition, selected work papers are also documented as having been reviewed. However, as previously explained to the SCO, it was not VTD's policy that every single work paper located in the file needed to contain the initial of the reviewer. Key audit areas can be sufficiently documented as being reviewed by indicating initials on the audit program and/or lead schedules or other documentation contained in the work papers. The policy was established by VTD and it is our opinion that all of the engagements, except EUSD 1997-98 are within our policy. We only agree with the SCO that the supervisory reviews of the EUSD 1997-98 engagement were not completely documented.

Finding 3 – Analytical Review Deficiencies in Planning

We disagree with the SCO that VTD did not consistently document analytical review procedures in planning the audits. We discussed this at length with the SCO representatives and provided written explanation of how we performed and documented our planning analytical review.

VTD utilized our review of the Second Interim Report during the interim phase of our audit as documented under the T5 section and appropriate procedures were performed as deemed necessary under the circumstances. During the early stages of the final phase of the audit, comparisons of current year financial data with prior year financial data and current year budgeted information is made as documented under the Revenue and Expenditures section of the audit. The comparison of current year to prior year and budgeted amounts was typically accomplished at the time financial data is entered into our trial balance and preliminary draft financial statements are prepared. We utilized variance reports of revenues and expenditures by fund where variances meet certain criteria to identify any additional accounts that need to be addressed which are not already planned procedures in our revenue and expenditure audit program and to provide for substantive analytical audit procedures for revenue and expenditures in addition to our specific testing of those areas outlined in our audit program and properly documented in the work papers.

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We believe these procedures comply with AU 329.01, which requires the performance of analytical procedures in the planning stage of the audit and that adequate documentation of these procedures were included in the work papers.

See the Appendix attached to this response for citations of standards related to the use of analytical review procedures in the planning stages of the audit.

Finding 4 – Deficiencies in consideration of Computer Processing System in Planning.

We agree with the SCO that the documentation of our consideration of computer process systems in planning could be enhanced. Consideration of the computer processing systems are typically addressed during the process of gaining an understanding of the internal controls over the various cycles (cash receipts, cash disbursements, payroll, etc.) This is accomplished through the use of internal control questionnaires, narratives, flow-charts, and other information. We agree that some of the files were not complete in documenting these processes. We have since revised our planning documents with regard to internal controls to further document the computer processing system.

Finding 5 – Internal Control Deficiencies

We disagree with the SCO that adequate documentation of our understanding of the control environment, accounting system, and control procedures was not provided in the work papers. We believe SCO reviewers have made assumptions that are not correct. The overall planning documentation assessed control risk at maximum, the assessment of control risk at maximum was not repeated at each audit section for account balance, disclosure components etc. An assessment of control risk at less than maximum would have been required to be documented in each section that varied from the overall assessment. All audit programs and procedures for each section did contemplate control risk at maximum.

During the time of these audits, VTD used an evaluation and planning form to document its understanding of the internal controls sufficient to plan the audit as required by AICPA and GAGAS. This form was developed using the Evaluation and Planning checklist from PPC and had been modified specifically for school districts. In addition, further understanding of the transaction cycles including cash receipts, cash disbursements, and payroll is obtained through the use of flowcharts, questionnaires, memos, and walkthroughs of the transaction cycles.

The report incorrectly cites AU 319.57 indicating that the auditor should document the basis for his or her conclusions about the assessed level of control risk. This citation has been taken out of context and does not apply under the circumstances. This section also states "...for those financial statement assertions where control risk is assessed at the maximum level, the auditor should document his conclusion that control risk is at the maximum level but need not document the basis for that conclusion." [Emphasis added] VTD documented that control risk was at the maximum level. There was no need for us to document our basis for this conclusion as the auditor was only required to do so in instances where control risk was assessed below maximum.

The report and summary of findings by district and year incorrectly refers to test of transactions. Because VTD indicated that control risk was assessed at maximum (i.e. evaluating the effectiveness of controls would be inefficient), there was no requirement for us to perform test of controls. Our limited testing of the controls are for the sole purpose of gaining a further understanding of the controls and not to place reliance on those controls or to provide support for an assessed level of control risk below maximum. AU 319.03 (as revised March 2003) requires testing of controls in instances where control risk is assessed below the maximum only, not when assessed at maximum.

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There is no standard that prevents an auditor from always assessing control risk at the maximum level. As cited in AU Section 319.03, the auditor may assess control risk at the maximum level if it is determined to be inefficient to evaluate the effectiveness of the controls. We have determined this to be the case in the majority of school district audits.

Finding 6 – Working Paper Deficiencies

We disagree with the SCO that there were numerous working paper deficiencies for each LEA audit reviewed. Many of the examples cited both in the report and the summary of findings by district and year and are not accurate portrayals of the working papers.

EUSD 1997-98

We disagree there was no explanation of the two adjusting journal entries. The total adjustment appears in the supplementary information section of the audit report. The two adjustments are supported by a copy of an invoice included in the work papers for the total amount of the two adjustments. In addition, as documented in the work papers, it was determined that the amount selected to verify as accounts payable for the building fund was not necessary since the adjustments noted during the subsequent testing far exceeded the amount that had been accrued, thus verification of the balances was already at 81%. We disagree that the financial statement documentation was deficient. Receivables, accounts payable and deferred revenues are supported by listings of the components of these balances along with significant substantive audit testing to verify the balances. State Revenue Limit Sources are supported by the recalculation of the recorded revenue limit using the forms provided with the second principal apportionment and updating for annual amounts. We do, however, agree with some of the items listed under the summary of findings by district by year.

EUSD 1998-99

We disagree with many of comments made by the SCO for EUSD FY 1998-99 in the report and the summary by district and year. For all key audit areas, lead sheets are included that agree to the balances on the financial statements. These lead sheets are referenced to detail listings prepared by the client and designated as such through the use of "PBC", a common designation for the client prepared documents. The detail listings include line items of the amounts and significant amounts were tested to verify the amounts were valid or referenced to other work papers where supporting documentation was included or additional recalculation of amounts was performed (for instance recalculation of accounts receivable, accounts payable and deferred revenue related to categorical programs and revenue limit sources). The agreement of account balances from the lead sheet and/or detail listings was made to the J200 as a means of verifying that the detail listing and related balances are in agreement with the amount that ultimately appeared on the financial statements. VTD believes the documentation for the account balances indicated in the examples is sufficient to support our opinion on the financial statements.

We disagree with the SCO that disclosure or accrual of the judgment noted was required under the circumstances. The auditor was aware of the situation, analyzed the amount in conjunction with other potential adjustments and determined and documented that adjustments were not necessary.

The SCO incorrectly refers to sampling methodology for instances where sampling methodology was not employed.

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FUSD 1999-2000

We disagree with the examples noted for FUSD 1999-2000. Cash and Investments presented on the lead sheets for all district funds and the ASB accounts agree to the consolidated footnote worksheet, which agrees to the financial statements. Therefore, no explanation was warranted. At the exit conference held in October 2003, the SCO representatives indicated this item would be removed from the report.

We disagree with the example for accounts payable. The additional amount of the liabilities is due to adjustments that were made to 3 individual funds. These adjustments were manually entered and the related accounts payable balances were indicated on the lead sheet. We agree that the total column amount had not been revised for the manual adjustments on the work paper. Manually adjusting the total column was not necessary to agree the worksheet to the financial statements and does not affect the ability of an experienced auditor from understanding the work paper. There was an explanation along with work papers to support the adjustments made. These adjustments were also presented in the supplementary information schedule in the audited financial statements and the trial balances for the individual funds also presented the unadjusted balances, the adjustment amounts and the report balances. In addition, included in the work papers is an AJE report that lists these three adjustments. We were under the impression that the SCO would not be including this as an example based upon discussions during the exit conference held in October 2003.

We agree there was an oversight and the amount indicated in the working papers was not properly updated for a change made on the report between the amount to be provided and the amount available.

We disagree with the comment regarding conclusions. Our audit programs contain standard conclusions referring to audit objectives. This is consistent with that used by Practitioner's Publishing Company (PPC), from which our school district audit programs were designed and we believe this is appropriate. The work papers referred to not having initials or dates relate to multiple pages of a report upon which is the initial and dates of the preparer and reviewer on at least one page of the multiple page report.

NUSD 1999-2000

We disagree with all but a few of the examples noted for NUSD 1999-2000. For all audit areas listed by the SCO, account balances and the related notes to the financial statements are supported by the lead schedules, which are further supported by the audit testing performed as documented in the work papers. Revenues and related accounts receivable, accounts payable, deferred revenue and restricted balances related to categorical programs are tested through verification of amounts presented on the J390 and recalculation of amounts. Through this testing we determined that the components of account balances and fund reservations were accurate and appropriate.

We do not agree that amounts were not verified or agreed to supporting documentation. An item of revenue was misclassified between state revenue limit and local property tax sources when the financial statements were prepared. The income was properly stated. The misclassification was not material and would not have affected the decisions of a reader of the financial statements. As documented in the working papers, all revenue limit sources were subjected to recalculation using the schedules contained in the second principal apportionment and taking into consideration changes for annual amounts that were then compared to recorded amounts.

We disagree that expenditures on the J200 do not agree with the financial statements. All expenditures as presented in the J200 are in agreement with those presented in the financial statements after taking into consideration adjustments and reclassifications as documented in the working papers.

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Response to quality review
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We agree that the work papers for the amounts presented for the joint powers authorities did not contain support. To provide efficiencies, we have developed a central file and spreadsheet for accumulating financial information about the joint power authorities. An example of this spreadsheet was provided to the SCO representatives and we were under the impression that this example would not be mentioned in the report.

Adequate testing for Federal grant awards was performed and documented in the working papers. It is not necessary to verify 100% of the Federal awards. Two of the programs listed by the SCO were major programs and documentation is included in the working papers that details the procedures performed and to support the recorded revenue and related accruals.

We disagree that disclosure was required for the item noted on the one attorney letter. The attorney letter indicated that the District would most likely prevail and no judgment had been made as of the date of our audit. This treatment is in accordance with FASB No. 5.

There would have been no value in performing a comparison of budget to actual. As can be seen from the budget to actual statements presented in the financial statements, the District revised its final budget to agree to actual amounts for almost all funds by major object. No variances would have been identified if the final budget amounts and the actual amounts were in agreement.

Finding 7 – Deficiencies in Evaluating Fraud, Illegal Acts, and Other Noncompliance

We disagree with the SCO that VTD did not adequately address potential fraud, illegal acts, or other noncompliance during the EUSD 1998-99 audit.

VTD used the Fraud Risk Assessment Worksheet to document its understanding of the potential for fraud on this engagement in accordance with SAS No. 82, GAGAS 4.12 c and 4.13. We believe that appropriate procedures were performed and appropriate documentation of those procedures were included in the work papers relating to the key people at the District and limitations for segregation of duties. Regarding the conflict of interest policy not being retained in the file – it is not necessary that every single answer to a question would result in the retention of documentation to support the answer to that question. At the time of the audit, it was determined that the retention of the conflict of interest policy would not enhance the audit. We do not understand why the SCO included the fifth paragraph under this finding. The evaluation and planning form clearly indicated that no modifications to our standard audit programs were planned. Obviously, had modifications to the standard audit programs been warranted under the circumstances, these would have been properly documented at the specific audit program. There is an audit step on each audit program to document additional audit procedures that may have been considered necessary. Had modifications been warranted they would have been documented on the audit program as planned as well as on any related work paper.

We disagree with the SCO that this represents an example of a deficiency in evaluating fraud, illegal acts, and other noncompliance.

Finding 8 – Reporting Deficiencies

The auditor's reports were correct. The reports should reflect the opinion of the auditor and did. It is not appropriate to determine a report deficiency because of deficiencies noted in other standards. To suggest that the report should have been modified to state that professional standards were not followed would also suggest that departures were known by the firm. If such departures had existed, our firm procedures would be to cure the departures not issue a modified report. Further, the deficiencies noted with which we agree would not be of such prevalence or significance to be considered a departure from professional standards that a report should be

State Controller's Office
Response to quality review
Page 8 of 12

modified in any event. To our knowledge the SCO found no instances of the District financial statements to be materially misleading.

Finding 9 – State Compliance Testing and Reporting Deficiencies

We agree with some of the items noted under this finding by the SCO, however, we disagree with other items noted.

EUSD 1997-98

We disagree with the example presented for EUSD for 1997-98 in the report. The procedures are documented by sign off of the audit steps on the audit program and review of the District calendar for the year. It was determined that additional physical documentation was not required as further evidence of the District's compliance. It was included at the step on the audit program that the auditor reviewed the site plan for determination of compliance. As noted in footnote 6 of GAGAS 4.37b, it was not necessary for the auditor to retain all copies of documentation used during the audit.

We disagree with the comments made under the summary by district and year for Staff Development Days, Kindergarten and Reading Instruction Development Program. Appropriate procedures were performed and documented in the working papers based upon what was determined appropriate under the circumstances. For instance, the Reading Development Program only spent \$2,900 and none was spent for grades 4 – 8. Also included in the working papers were Core agendas and the scope of work to indicate the training topics as additional supporting documentation. We agree only with the comments regarding lack of documentation for the Gann Limit.

EUSD 1998-99

For EUSD 1998-99 we agree with the items noted regarding Kindergarten Enrollment and Staff Development Days, however, we disagree with the item noted regarding Class Size Reduction Program. The requirement is for the auditor to select at least 15 days at random selecting from instructional days between the first day of instruction and April 15. We acknowledge that one of the days selected should not have been selected, however, the other days selected were within the period required for selection. Had the maximum average class size been exceeded for the classes selected for testing based upon the 15 days tested, further investigation would have been performed and the average would have been calculated from the first day of instruction through April 15th to ensure compliance. None of the classes exceeded the maximum average; therefore, additional testing was not warranted. The SCO also notes that the working papers indicated there should be a revision. The revision would have been to the benefit of the District. This would have been communicated to management and it would be up to them to prepare the revision. Follow up was not considered necessary under the circumstances.

We agree with some of the additional items noted in the summary by district and year as noted above, however, we believe the testing on the Gann Limit was appropriate and well documented under the circumstances.

EUSD 1999-2000

We agree with the minutes calculated by SCO representatives. We also agree with the additional comments made under the summary by district and year.

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FUSD 1999-2000

We disagree with the conclusion made by SCO that staff development days should have been disallowed for the days marked as "undecided". As can be seen in the work papers, the dates marked as "undecided" were scheduled subsequent to the audit date of this section. The school district maintains adequate documentation to support their staff development days. Had the days occurred prior to the audit date, the auditor would have requested and reviewed the appropriate documentation. The SCO cannot make such a conclusion based solely on our audit documentation as the test was performed prior to the dates.

NSUD 1999-2000

We disagree with the comments made regarding the K-3 Class Size Reduction (Option 1). Alternative procedures were performed and properly documented in the work papers. Daily count sheets were used in lieu of the selection of 15 days, in essence, providing 100% daily testing rather than a selected 15 days.

We disagree with the comments regarding Morgan Hart Class Size Reduction. There was a finding included in the audit report regarding the lack of documentation available. This was the issue that existed at the time of our audit report. The District provided some information subsequent to the audit that indicated there was a misstatement of 3 FYEE, however, all of the documentation to support this misstatement was not provided until well after issuance of the report. Follow up was performed as part of the audit for 2000-01 and the finding was indicated as implemented after all supporting documentation had been provided for our review.

We disagree with the additional comments in the summary by district and year for Staff Development, Incentives for Longer Instructional Day, and State Instructional Materials fund. We were under the impression that the SCO representatives were satisfied with the issues related to the Staff Development comment and that the comment would not appear in the next draft of the report. Documents were included in the work papers and proper references were provided. The SCO has incorrectly assumed that the 25 referred to minimum days. It did not; it referred to the number of regular school days in the November/December time frame that is a component of the total 137 regular days. The minutes were appropriately calculated. The verification of the resolution for the sufficiency of instructional materials is further documented in the excerpts to the minutes of the board meetings dated June 20, 2000.

Mission Valley ROP 1999-2000

We disagree with the comments made regarding the testing of attendance reports. There is documentation on the work papers to indicate that amounts were traced and agreed to monthly ADA reports and that the auditor added the hours from the ADA reports. In addition, the selection of sample classes and agreement to monthly totals were performed and documented. We believe the evidence in the working papers support these audit steps. We agree the report should have been modified for lack of testing excused absences.

Finding 10 – State Compliance Sample Selection Deficiencies and Expansion of Testing

We agree that the documentation for sampling for state compliance testing was not always well documented. In some of the instances cited, however, the auditor did document that the exception was determined to be isolated and therefore, did not perform additional testing as it was not deemed necessary.

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Finding 11 – Federal Program Internal Control Deficiencies

We disagree with all comments for this finding that SCO has included its summary of findings by district and year. The comments made are inaccurate. In addition, all references that SCO makes in Finding 8 regarding standards contained in OMB Circular A-133, *Audits of State, Local Governments, and Non-Profit Organizations* (A-133) and references to Findings 11 are also inaccurate. VTD complied with requirements under A-133 and, therefore, none of our reports required under A-133 are misleading.

We only agree with the SCO regarding the EUSD 1999-2000 that the internal control checklist was incorrectly marked as low rather than moderate. However, the procedures performed were proper for a moderate level assessment as the auditee was indicated as not low risk and programs tested were at the 50% testing level. We believe this is a minor deviation and the audit was not deficient as the result of the incorrect marking of the risk on the questionnaire.

We disagree with all other comments the SCO has made under this finding. The Compliance Memos for each of the major programs provide documentation of our understanding of the internal controls for NUSD. These memos were located in the Single Audit section of the audit and made available to the SCO representatives for their review. Included in each of these memos is our understanding of the five components of internal control over compliance for the applicable 14 compliance items. The SCO incorrectly refers to documents in the audit working papers that were used for other purposes during the course of the audit or to documents that were not intended for the 1999-2000 audit.

VTD performed procedures to obtain an understanding of the internal control over compliance, VTD planned tests of controls, and VTD performed tests of internal control as documented in the working papers at the Single Audit section.

We have appropriately documented our understanding of the internal controls over the applicable compliance areas that are relevant to its major programs as documented through the use of questionnaires and memos. In addition, appropriate testing of those controls was performed and properly documented in the work papers.

Finding 12 – Federal Program Compliance Deficiencies

We disagree with all comments for this finding that SCO has included its Summary of Findings by District and Year. The comments made are inaccurate. In addition, all references that SCO makes in Finding 8 regarding standards contained in OMB Circular A-133, *Audits of State, Local Governments, and Non-Profit Organizations* (A-133) and references to Findings 12 are also inaccurate. VTD complied with requirements under A-133 and, therefore, none of our reports required under A-133 are misleading.

SCO has incorrectly applied Single Audit Requirements in arriving at its conclusion with respect to programs being audited. **OMB Circular A-133.520** requires auditors to use a risk-based approach to determine which Federal programs will be tested as Major programs. This is accomplished by first grouping federal programs by Type A (\$300,000 in the case of the districts reviewed) and Type B programs (less than \$300,000). The next step is to identify low-risk Type A programs (those programs audited as major in at least one of the two most recent periods and had no audit findings). The third step is to identify any Type B programs, which are high-risk (excluding those programs that do not exceed \$100,000. After the risk assessment has been made the auditor than selects to test as major programs all Type A programs (but may exclude any Type A programs that are low-risk) and any Type B programs that have been identified as high-risk. Additional programs may need to be selected in order to achieve the appropriate percentage coverage (25% for low-risk auditees and 50% for those not qualifying as low-risk).

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VTD has complied with this requirement as documented in our work papers and all programs that should have been identified as major were identified as such and appropriate testing was performed. There is no requirement that the auditor apply tests to any programs not identified as "major".

In addition, SCO has incorrectly applied Single Audit Requirements with respect to the need to perform compliance tests for all of the 14 compliance areas identified in the OMB Compliance Supplement and has listed our audit program for the Child Nutrition Cluster as an example. The Introduction in Part 2 – Matrix of Compliance Requirements of the OMB A-133 Compliance Supplement indicates "Even though a "Y" indicates that a compliance requirement applies to the Federal program, it may not apply at a particular non-Federal entity, either because that entity does not have activity subject to that type of compliance requirement or the activity could not have a material effect on a major program." This paragraph also states "The auditor should exercise professional judgment when determining which compliance requirements marked "Y" need to be tested at a particular non-Federal entity."

VTD has followed this guidance in developing its audit program for the Child Nutrition Cluster. We have used Part 3 and Part 4 as indicated in the introduction paragraph of Part 2 in developing our audit program and determining which of the 14 compliance requirements are applicable or material to the Child Nutrition Cluster.

The SCO cites Cash Management as an item that we have indicated as not being applicable. Cash Management requirements and recommended procedures are found in Part 3 of the Compliance Supplement. This compliance requirement pertains to federal funds received in advance or in situations where reimbursements are based upon expenditures being made in advance of the reimbursement request. This compliance requirement is not applicable to the Child Nutrition program because the reimbursement is based upon meals served and not expenditures made. This requirement also pertains to interest earned on federal funds received in advance. Since the District does not receive any funds in advance, this requirement is not applicable. This should be obvious to anyone who is familiar with the Child Nutrition Cluster.

The SCO cites Equipment and Real Property as an item that we have indicated as not being applicable. This compliance requirement pertains to equipment and real property purchased with Federal funds and can be found in Part 3. Since the District did not purchase any equipment and real property, it is obvious that this requirement was not applicable.

The SCO cites Program Income as an item that we have indicated as not being applicable. This compliance requirement pertains to gross income received that is directly generated by the federally funded program where certain amounts (such as fees for services performed or the use or rental of real or personal property). In these instances, the program income is deducted from the amount of federal awards or used as matching funds. Since the Child Nutrition Cluster only provides for the reimbursement based upon meals served, it is obvious that this item is not applicable.

The SCO cites Reporting as an item that we have indicated as not being applicable. The compliance requirement pertains to specific reports as identified in Part 3 and Part 4 that are not applicable to the District's Child Nutrition Program. Part 4 includes the testing of reports for reimbursement claims under Activities Allowed or Unallowed. It is not necessary to state why this is not applicable as it is clearly indicated in Parts 3 and Parts 4.

The SCO cites Subrecipient Monitoring as an item that we have indicated as not being applicable. The compliance requirement pertains only to State agencies and can be found in Part 4. It is not necessary to state why this is not applicable as it is clearly indicated in Part 4 that it only applies to State agencies.

The SCO cites Procurement and Suspension and Debarment (NUSD Only). The audit program for the National School Lunch Program is clearly identified as to why this compliance requirement is not applicable. Since at the

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time of the audit, all expenditures for the Special Education Program were related to salaries and benefits, it was not likely that this compliance item being material to that program. Again, this would be obvious to anyone familiar with the Special Education Program.

In designing its program for the Child Nutrition Program, VTD complied with the requirements of OMB A-133.520 and all procedures that were applicable and material to the programs were audited accordingly.

Conclusion

In conclusion, we request SCO representatives to contact us should further revisions to the draft report be made prior to its issuance in final form. We request the opportunity to revise our response accordingly for any revisions made by SCO. In addition, we request the SCO include our response in its entirety along with the distribution of the SCO report. Should the SCO post its report on their website or in anyway distribute its report electronically, we request our response accompany such posting and distribution.

Sincerely,



Linda S. Todd
of Vavrinek, Trine, Day & Co., LLP

LST:lst

Appendix attached

Appendix

Additional Information and Applicable Standards By Finding

Finding 1 – Due Professional Care – Additional Information and Applicable Standards

Following are applicable standards and other information regarding scope limitations and materiality:

Materiality

PPC – 406.21 - Planning materiality applies to the fund type, fund, or opinion unit financial statements taken as a whole. Planning materiality is the acceptable limit on misstatement of financial statements. In this sense, it is a “cushion” that the auditor allows for the necessary imprecision in applying auditing procedures to detect misstatement of the financial statements; i.e., an allowance for undetected misstatement. Tolerable misstatement applies at the account balance level and is the allowance for undetected misstatement at that level.

AU 312.10 - The auditor's consideration of materiality is a matter of professional judgment and is influenced by his or her perception of the needs of a reasonable person who will rely on the financial statements. The perceived needs of a reasonable person are recognized in the discussion of materiality in Financial Accounting Standards Board Statement of Financial Accounting Concepts No. 2, Qualitative Characteristics of Accounting Information, which defines materiality as "the magnitude of an omission or misstatement of accounting information that, in the light of surrounding circumstances, makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or misstatement." That discussion recognizes that materiality judgments are made in light of surrounding circumstances and necessarily involve both quantitative and qualitative considerations.

AU 312.12 - The auditor should consider audit risk and materiality both in (a) planning the audit and designing auditing procedures and (b) evaluating whether the financial statements taken as a whole are presented fairly, in all material respects, in conformity with generally accepted accounting principles. The auditor should consider audit risk and materiality in the first circumstance to obtain sufficient competent evidential matter on which to properly evaluate the financial statements in the second circumstance.

AU 312.14 *Section 311, Planning and Supervision*, requires the auditor, in planning the audit, to take into consideration, among other matters, his or her preliminary judgment about materiality levels for audit purposes. That judgment may or may not be quantified.

AU 312.15 According to section 311, the nature, timing, and extent of planning and thus of the considerations of audit risk and materiality vary with the size and complexity of the entity, the auditor's experience with the entity, and his or her knowledge of the entity's business. Certain entity-related factors also affect the nature, timing, and extent of auditing procedures with respect to specific account balances and classes of transactions and related assertions. (See paragraphs .24 through .33.)

AU 312A.03 The concept of materiality recognizes that some matters, either individually or in the aggregate, are important for fair presentation of financial statements in conformity with generally accepted accounting principles, while other matters are not important. The representation in the auditor's standard report regarding fair presentation, in all material respects, in conformity with generally accepted accounting principles indicates the auditor's belief that the financial statements taken as a whole are not materially misstated.

AU 312A.19 - In planning the audit, the auditor should use his or her judgment as to the appropriately low level of audit risk and his or her preliminary judgment about materiality levels in a manner that can be expected to provide, within the inherent limitations of the auditing process, sufficient evidential matter to obtain reasonable assurance about whether the financial statements are free of material misstatement. Materiality levels include an

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Additional Information and Applicable Standards By Finding

overall level for each statement; however, because the statements are interrelated, and for reasons of efficiency, the auditor ordinarily considers materiality for planning purposes in terms of the smallest aggregate level of misstatements that could be considered material to any one of the financial statements. For example, if the auditor believes that misstatements aggregating approximately \$100,000 would have a material effect on income but that such misstatements would have to aggregate approximately \$200,000 to materially affect financial position, it would not be appropriate for him or her to design auditing procedures that would be expected to detect misstatements only if they aggregate approximately \$200,000.

AU312A.20 - The auditor plans the audit to obtain reasonable assurance of detecting misstatements that he or she believes could be large enough, individually or in the aggregate, to be quantitatively material to the financial statements. Although the auditor should be alert for misstatements that could be qualitatively material, it ordinarily is not practical to design procedures to detect them. Section 326, Evidential Matter, states that "an auditor typically works within economic limits; his or her opinion, to be economically useful, must be formed within a reasonable length of time and at reasonable cost."

AU9312A 4.16 - Interpretation—Section 312A.10 states that the auditor's consideration of materiality is a matter of professional judgment and is influenced by his or her perception of the needs of a reasonable person. Section 312A.11 states—As a result of the interaction of quantitative and qualitative considerations in materiality judgments, misstatements of relatively small amounts that come to the auditor's attention could have a material effect on the financial statements. For example, an illegal payment of an otherwise immaterial amount could be material if there is a reasonable possibility that it could lead to a material contingent liability or a material loss of revenue. Section 508, Reports on Audited Financial Statements, paragraph .36, states that the significance of an item to a particular entity (for example, inventories to a manufacturing company), the pervasiveness of the misstatement (such as whether it affects the amounts and presentation of numerous financial statement items), and the effect of the misstatement on the financial statements taken as a whole are all factors to be considered in making a judgment regarding materiality. Section 312A.10 also makes reference to the discussion of materiality in Financial Accounting Standards Board Statement of Financial Accounting Concepts No. 2, Qualitative Characteristics of Accounting Information. FASB Concepts Statement No. 2, paragraphs 123 through 132, includes a discussion about matters that might affect a materiality judgment.

Scope Limitations

AU 508.22 The auditor can determine that he or she is able to express an unqualified opinion only if the audit has been conducted in accordance with generally accepted auditing standards and if he or she has therefore been able to apply all the procedures he considers necessary in the circumstances. Restrictions on the scope of the audit, whether imposed by the client or by circumstances, such as the timing of his or her work, the inability to obtain sufficient competent evidential matter, or an inadequacy in the accounting records, may require the auditor to qualify his or her opinion or to disclaim an opinion. In such instances, the reasons for the auditor's qualification of opinion or disclaimer of opinion should be described in the report. [Paragraph renumbered by the issuance of Statement on Auditing Standards No. 79, December 1995.]

AU508.23 The auditor's decision to qualify his or her opinion or disclaim an opinion because of a scope limitation depends on his or her assessment of the importance of the omitted procedure(s) to his or her ability to form an opinion on the financial statements being audited. This assessment will be affected by the nature and magnitude of the potential effects of the matters in question and by their significance to the financial statements. If the potential effects relate to many financial statement items, this significance is likely to be greater than if only a limited number of items is involved. [Paragraph renumbered by the issuance of Statement on Auditing Standards No. 79, December 1995.]

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AU326.22 The independent auditor's objective is to obtain sufficient competent evidential matter to provide him or her with a reasonable basis for forming an opinion. The amount and kinds of evidential matter required to support an informed opinion are matters for the auditor to determine in the exercise of his or her professional judgment after a careful study of the circumstances in the particular case. However, in the great majority of cases, the auditor has to rely on evidence that is persuasive rather than convincing. Both the individual assertions in financial statements and the overall proposition that the financial statements as a whole are fairly presented are of such a nature that even an experienced auditor is seldom convinced beyond all doubt with respect to all aspects of the statements being audited. [Paragraph renumbered by the issuance of Statement on Auditing Standards No. 48, July 1984. Paragraph subsequently renumbered and amended, effective for engagements beginning on or after January 1, 1997, by the issuance of Statement on Auditing Standards No. 80.]

AU326.23 An auditor typically works within economic limits; the auditor's opinion, to be economically useful, must be formed within a reasonable length of time and at reasonable cost. The auditor must decide, again exercising professional judgment, whether the evidential matter available to him or her within the limits of time and cost is sufficient to justify expression of an opinion. [Paragraph renumbered by the issuance of Statement on Auditing Standards No. 48, July 1984. Paragraph subsequently renumbered by the issuance of Statement on Auditing Standards No. 80, December 1996.]

AU326.24 As a guiding rule, there should be a rational relationship between the cost of obtaining evidence and the usefulness of the information obtained. The matter of difficulty and expense involved in testing a particular item is not in itself a valid basis for omitting the test. [Paragraph renumbered by the issuance of Statement on Auditing Standards No. 48, July 1984. Paragraph subsequently renumbered by the issuance of Statement on Auditing Standards No. 80, December 1996.]
Evaluation of Evidential Matter

AU326.25 In evaluating evidential matter, the auditor considers whether specific audit objectives have been achieved. The independent auditor should be thorough in his or her search for evidential matter and unbiased in its evaluation. In designing audit procedures to obtain competent evidential matter, he or she should recognize the possibility that the financial statements may not be fairly presented in conformity with generally accepted accounting principles or a comprehensive basis of accounting other than generally accepted accounting principles. fn 3 In developing his or her opinion, the auditor should consider relevant evidential matter regardless of whether it appears to corroborate or to contradict the assertions in the financial statements. To the extent the auditor remains in substantial doubt about any assertion of material significance, he or she must refrain from forming an opinion until he or she has obtained sufficient competent evidential matter to remove such substantial doubt, or the auditor must express a qualified opinion or a disclaimer of opinion. fn 4 [Paragraph renumbered by the issuance of Statement on Auditing Standards No. 48, July 1984. Paragraph subsequently renumbered and amended, effective for engagements beginning on or after January 1, 1997, by the issuance of Statement on Auditing Standards No. 80.]

Finding 3 – analytical Review Deficiencies in Planning

Following are applicable sections of auditing standards related to using analytical review in the planning stages of the audit:

AU 329.04 Analytical procedures are used for the following purposes:

- a. To assist the auditor in planning the nature, timing, and extent of other auditing procedures
- b. As a substantive test to obtain evidential matter about particular assertions related to account balances or classes of transactions
- c. As an overall review of the financial information in the final review stage of the audit

Analytical procedures should be applied to some extent for the purposes referred to in (a) and (c) above for all audits of financial statements made in accordance with generally accepted auditing standards. In addition, in

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some cases, analytical procedures can be more effective or efficient than tests of details for achieving particular substantive testing objectives.

Analytical Procedures in Planning the Audit

AU 329.06 The purpose of applying analytical procedures in planning the audit is to assist in planning the nature, timing, and extent of auditing procedures that will be used to obtain evidential matter for specific account balances or classes of transactions. To accomplish this, the analytical procedures used in planning the audit should focus on (a) enhancing the auditor's understanding of the client's business and the transactions and events that have occurred since the last audit date, and (b) identifying areas that may represent specific risks relevant to the audit. Thus, the objective of the procedures is to identify such things as the existence of unusual transactions and events, and amounts, ratios and trends that might indicate matters that have financial statement and audit planning ramifications.

AU 329.07 Analytical procedures used in planning the audit generally use data aggregated at a high level. Furthermore, the sophistication, extent and timing of the procedures, which are based on the auditor's judgment, may vary widely depending on the size and complexity of the client. For some entities, the procedures may consist of reviewing changes in account balances from the prior to the current year using the general ledger or the auditor's preliminary or unadjusted working trial balance. In contrast, for other entities, the procedures might involve an extensive analysis of quarterly financial statements. In both cases, the analytical procedures, combined with the auditor's knowledge of the business, serve as a basis for additional inquiries and effective planning.

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Attachment 2— SCO's Comments Regarding Firm's Response

FINDING 1—Due professional care

The SCO's comments to specific issues addressed by VTD are as follows:

Inventory

The SCO did not make assumptions regarding materiality. The SCO's comments regarding materiality were based on information presented in VTD's working papers, additional written information provided, discussions with VTD staff, and professional standards.

In performing the audit, VTD did not address why the stores inventory balance remained the same for two consecutive fiscal years.

Further, for EUSD FY 1999-2000, VTD's working papers stated that the determined amount for materiality was \$10,700. In addition, the working papers did not support VTD's conclusion that inventory records were unauditable. A finding was not reported and there was no scope limitation.

Payroll Clearing Account

VTD indicated that there was no payroll clearing account on the audit program for revenues and expenditures. The audit program identifies specific audit procedures to be performed during substantive testing. Although VTD may not have been aware of the existence of a payroll clearing account during interim work, VTD should have noted the payroll clearing account at the time substantive testing was performed, and revised the audit program accordingly. In addition, there was no documentation in the working papers indicating that the specific audit procedures, detailed in the audit program and related to the payroll clearing account, were performed.

Deficient Attendance Testing

The summary planning document discussed by VTD was not noted in the working papers during the SCO's review, and VTD did not provide a copy of this document to the SCO during subsequent discussions. There was no documentation in the working papers indicating why the number of sites originally selected for testing on the Attendance Control Sheet in the system file was revised.

FINDING 2—Quality control deficiencies

As noted in the examples detailed in the Summary of Findings by District and Year, VTD did not consistently review and sign off on key audit areas in accordance with VTD's established policy.

FINDING 3—Analytical review deficiencies

Although VTD provided additional information regarding analytical review procedures during discussions subsequent to the SCO's review, and in writing, not all of the working papers for the individual audits contained evidence that analytical reviews were performed in planning the audits. The SCO agrees that for some districts and years reviewed, an analytical review was performed in the final review stage of the audits; however, professional standards require that an analytical review also should be performed in the planning stages.

FINDING 4—Deficiencies in consideration of computer processing system in planning

VTD agrees with the finding.

FINDING 5—Internal control deficiencies

SAS 78 specifically requires that the auditor assess control risks for the assertions embodied in the account balance, transaction class, and disclosure components of the financial statements. VTD did not document this in the working papers.

VTD states that the summary of findings “incorrectly refers to test of transactions.” However, VTD’s working papers contained audit programs titled “Walkthrough and Tests of Transactions” for various accounts. The SCO agrees that VTD performed only limited testing of controls. However, the SCO’s concern was that when exceptions were noted during the walkthroughs or tests of controls, VTD did not evaluate the discrepancy or report an internal control finding.

It should be noted that the SCO did not determine that VTD’s assessment of control risk at maximum violated auditing standards. However, it is more appropriate to evaluate control risk individually for each district to be audited, rather than to routinely assess control risk at the maximum level for all districts.

VTD cites AU 314.03 (as revised March 2003). However, the revised standard did not apply to the fiscal years of the audits reviewed.

FINDING 6—Working paper deficiencies

The SCO’s comments to specific issues addressed by VTD are as follows:

EUSD 1997-98

The working papers did not contain adequate explanations for the adjusting journal entries in question. The SCO agrees that the audit report reflects the adjustment; however, there was no documentation that the proposed adjustment was provided to the district or reflected in the district’s books.

Although VTD provided an explanation in its response to the finding of its rationale related to the Building Fund accounts payable accrual, this information was not documented in the working papers, nor was this information provided during discussions with VTD. In addition, VTD noted on the original draft report that it agrees with this finding.

The SCO maintains that the financial statement account balances noted in the finding were not adequately supported in the working papers. The documentation related to these accounts was not sufficient to enable the SCO reviewers to ascertain that the amounts reported were supported by adequate evidence.

EUSD 1998-99

The SCO maintains that the financial statement account balances noted in the finding were not adequately supported in the working papers. The working papers related to these accounts did not contain documentation of the work performed by VTD to substantiate the amounts reported.

In regard to the issue related to the contingent liability disclosure, the SCO maintains that the working papers did not contain evidence that VTD analyzed the amount and determined that an adjustment was not necessary.

The SCO disagrees with VTD's statement that the SCO incorrectly refers to sampling methodology for instances where sampling methodology was not employed. The working papers for deferred revenue indicated that 6 of 28 items listed on a worksheet were tested. AU 350.01 states, in part, "Audit sampling is the application of an audit procedure to less than 100 percent of the items within an account balance or class of transactions for the purpose of evaluating some characteristic of the balance or class." Therefore, sampling methodology would apply in this instance, and the working papers should have described the sampling methodology.

FUSD 1999-2000

The SCO maintains that the financial statement amounts noted in the finding were not adequately supported in the working papers. The working papers related to these accounts did not contain documentation of the work performed by VTD to substantiate the amounts reported.

For cash and investments, the amounts presented in the financial statements could not be traced to the working papers without additional verbal explanation by VTD. The SCO indicated that this item might be removed from the report; however, upon further review, the SCO concluded that the amounts reported could not be determined from the review of working papers alone.

For the accounts payable example, VTD made a notation in writing on a preliminary copy of findings presented at the exit conference indicating, "Agree – Correction made on financials wps were not updated for chg." Therefore, the example was included in this report.

The SCO's comment regarding conclusions was included because VTD did not revise the standardized conclusions contained in audit programs to accurately reflect the actual results of testing. Therefore, in some cases, the conclusions were not useful in determining whether the audit objectives for a particular area had been met. In addition, the SCO maintains that initials and dates of the preparer and reviewer were missing from several state compliance working papers that were not a part of multiple pages.

NUSD 1999-2000

The SCO maintains that the account balances and notes identified in the finding were not adequately supported in the working papers. The working papers related to these accounts and notes did not contain adequate documentation of the work performed by VTD to substantiate the amounts reported.

VTD states in its response that an item of revenue was misclassified; therefore, the amounts reported did not agree with supporting documentation. However, this was not documented in the working papers.

VTD further states that expenditures agree with the financial statements after considering adjustments and reclassifications; however, the adjustments and reclassifications were not documented in the working papers.

The SCO acknowledges that VTD has revised its procedures regarding testing of joint power authorities; however, at the time of the SCO review, the working papers did not contain supporting documentation.

The SCO agrees that it is not necessary to verify 100% of the federal awards; however, for those programs selected for testing, the reported amounts should be verified by tracing to the grant award or other supporting documentation. This was not documented in the working papers for any of the programs identified in the finding, including major programs.

With regard to the legal representation letter, there was no documentation in the working papers supporting VTD's analysis of the potential liability. Therefore, the SCO reviewers were unable to determine whether VTD's decision not to disclose was appropriate.

There was no documentation in the working papers supporting VTD's decision not to perform an analysis of budget to actual amounts. Therefore, the SCO reviewers were unable to determine whether VTD's decision not to perform this procedure was appropriate.

FINDING 7—Deficiencies in evaluating fraud, illegal acts, and other noncompliance

The SCO stands by its finding that VTD did not adequately address potential fraud, illegal acts, or other noncompliance in the working papers.

VTD identified that there was limited segregation of duties at the district, and district management was dominated by a single individual or small group; however, without compensating controls, there was a much higher risk of fraud occurring and not being detected. There was no evidence in the working papers that VTD adequately addressed potential fraud, illegal acts, or other noncompliance, or expanded or modified audit procedures to obtain more persuasive evidence. The Summary of Findings by District and Year provides additional examples of deficiencies in evaluating fraud, illegal acts, and other noncompliance.

The SCO's concern regarding the conflict of interest policy was that there was no documentation in the working papers indicating that the policy had been reviewed or evaluated by VTD. The SCO did not imply that VTD was required to retain a copy of the policy in the working papers.

As stated previously, there was limited segregation of duties at the district, and control was in the hands of two key people, without compensating controls. Accordingly, VTD should have expanded or modified audit procedures to obtain more persuasive evidence.

FINDING 8—Reporting deficiencies

The SCO did not suggest that the audit reports in question be modified. However, in the future, VTD should ensure that all applicable standards are followed, and if not, the audit reports should be modified accordingly.

FINDING 9—State compliance testing and reporting deficiencies

The SCO comments to specific issues addressed by VTD are as follows:

EUSD 1997-98

Staff Development Days: There was no evidence in the working papers that VTD selected a sample of two staff development days and determined that the days agreed to the school site plan, as required by the audit program. This procedure was referenced to the school calendar with no evidence of testing. In addition, there was no evidence in the working papers that VTD determined that the day before or the day after the staff development day was used for apportionment purposes, and 100% of attendance was not taken. An auditor's note on the audit program indicated, "Andrea uses the best of day before or day after." This is not sufficient to indicate that the procedure was performed as required.

Kindergarten Enrollment: The SCO disagrees that appropriate procedures were performed and documented in the working papers. An auditor's note on the audit program indicated, "Auditor verified all K student met the birthday requirement." However, the program was not referenced to supporting documentation, and there was no indication of the scope and methodology of testing. In addition, there was no evidence that the auditor compared current and prior year enrollment lists to identify kindergarten students who were retained. An auditor's note on the audit program indicated, "N/A, no kind. Retained from P/Y." However, there was no evidence supporting this statement, and the audit report was not modified to reflect that this procedure was not performed.

Reading Instruction Development Program: The SCO disagrees that the amount spent by the district should influence procedures performed. The procedures focus on compliance with program requirements, and amounts spent would not affect the procedures. The working papers did not contain documentation indicating that VTD verified that funds were used only to provide training to teachers and school site administrators. In addition, the working papers did not contain documentation supporting how VTD determined that the training did not cause a reduction in pupil instruction time, other than an auditor's note that, according to district staff, no reduction occurred.

EUSD 1998-99

VTD agreed with or did not address the specific examples identified, with the exception of the following items.

Class Size Reduction Program: The audit procedure addressed specifically states that the sample should be randomly selected. Random selection is used to ensure that the sample can be expected to be representative of the population. Therefore, all items in the population should have an opportunity to be selected. The sample selected by VTD did not meet the requirements of the audit procedure; therefore, the conclusions reached by VTD may not have been valid. In regard to the revision noted in the working papers, the reason for the revision and disposition was not documented.

Gann Limit Calculation: As noted in the SCO's finding, there was no documentation in the working papers supporting whether the auditor verified that the data used by the district was accurate, and ensured that the prior year ADA used by the district matched the data on the prior year calculation previously submitted to the State.

EUSD 1999-2000

VTD agreed with or did not comment on the findings presented.

VTD did not comment on the following findings except for the items listed.

FUSD 1999-2000

Staff Development Days: It was not evident from the working papers that the "undecided" dates were not within the period to be tested. According to the FUSD audit report, the last day of fieldwork was October 20, 2000. The "undecided" dates occurred prior to this. Therefore, due professional care requires that VTD should have requested and reviewed documentation related to these dates. It was poor auditor judgment to select a sample of staff development days to test that are outside of the fieldwork date, and then conclude that the district was in compliance with state requirements.

NUSD 1999-2000

Class Size Reduction Program: If alternative procedures were performed, the auditor's report on state compliance should have been modified accordingly. In addition, the sample selected may not have been representative of all instructional days as required.

Morgan Hart Class Size Reduction: The SCO's comment that no finding was reported referred to the overclaimed enrollment, not the lack of documentation. It was not evident from the working papers that the issue regarding the overclaimed attendance was identified subsequent to the audit. VTD did not provide other information or documentation regarding this during or subsequent to the review.

Staff Development: Upon further review of the working papers, the SCO reviewers concluded that the working papers did not contain sufficient information as evidence that all required procedures were performed.

Incentives for Longer Instructional Days: Upon further review of the working papers, the SCO reviewers identified other errors in VTD's calculations. Therefore, the number of instructional minutes reported was incorrect.

State Instructional Materials Fund: Upon further review of the working papers, the SCO reviewers noted there was no reference to the board meeting minutes in the working papers. Excerpts of the minutes of the board meetings were provided; however, there was no documentation indicating that VTD determined whether the district board made a determination through a resolution, as required.

Mission Valley ROP 1999-2000

The documentation in the working papers was insufficient to support the testing of the attendance reports. The working papers did not identify the specific numbers traced and the dates of the reports being reviewed.

The working papers indicated that ten students were tested; however, the documentation in the working papers was insufficient to support that the required procedures were performed. The working papers did not identify the specific monthly totals traced, did not identify the specific attendance records which the monthly totals were to be traced to, and did not specify that the attendance records were footed and cross-footed, as required.

FINDING 10—State compliance sample selection deficiencies and expansion of testing

The SCO identified several instances where VTD determined that an exception was isolated and no additional testing was performed. However, this conclusion was not appropriate, based on the sample size and error rate. For example, for EUSD FY 1998-99, for the State Instructional Materials Fund, one out of four transactions tested (25%) was noncompliant; however, VTD concluded that the district appeared to be in compliance. For EUSD FY 1999-2000, for Attendance Accounting–Excused Absence testing, one out of five students tested (20%) was noncompliant; however, VTD determined that this was an isolated incident. The fact remains that VTD's sample selections were inadequate to determine compliance with state program requirements.

FINDING 11—Federal program internal control deficiencies

Documentation related to federal program internal control was incomplete or not provided in the working papers for the districts and years cited in the report.

OMB Circular A-133 specifically requires that the auditor perform procedures to support a low assessed level of control risk for major programs and for the assertions relevant to the compliance requirements, and perform testing of internal control.

In addition, VTD agreed with specific federal program internal control deficiencies presented in the original draft report. For example, for EUSD FY 1999-2000, VTD noted on the draft report, "Agree that questionnaire should have indicated moderate." This was in response to a finding that the single audit control risk was assessed at low. Also, for NUSD FY 1999-2000, VTD noted on the draft report, "Agree not signed off as being updated for 2000," in response to the finding that the Planning Federal Programs questionnaire was not referenced to the year being audited.

FINDING 12—Federal program compliance deficiencies

VTD identified Type A federal programs; however, documentation in the working papers was insufficient to determine whether VTD identified low-risk Type A programs or high-risk Type B programs. Although testing of only Type A federal programs may have been appropriate, without adequate documentation, the SCO reviewers were unable to determine whether this was the case.

With regard to the 14 types of compliance requirements, the working papers did not provide an explanation or justification when a specific compliance requirement was considered not applicable. Therefore, the SCO reviewers were unable to determine whether VTD's decision not to test a specific requirement was appropriate.

In addition, during discussions with firm representatives, VTD stated that its approach was to determine which compliance requirements applied on a global basis rather than an LEA-by-LEA basis. It is more appropriate to evaluate whether the compliance requirements apply on a per LEA basis so that a complete and thorough audit of federal programs is performed.

Further, VTD made a hand-written notation on its copy of the original draft report that the firm had not adequately documented an explanation or justification when a specific compliance requirement was considered not applicable, but would do so in the future.

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